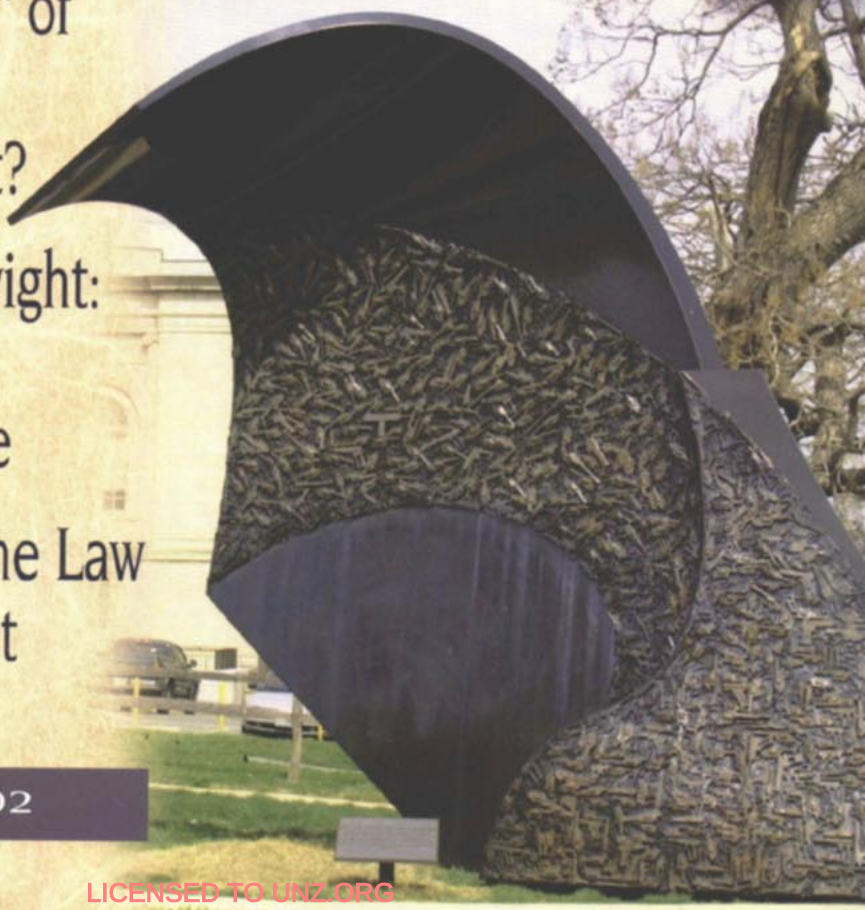
# IDEAS ON LIBERTY

FEE's Monthly Magazine

FEE Today: How YOU Can Fight the War on Terrorism

- Taxes into Plowshares
- The "Return" of Activist Government?
- Charlotte Twight: Designing Dependence
- Enron and the Law of the Market



MAY 2002

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# FEE SPAN!

As this issue of *Ideas on Liberty* was going to press, Mark Skousen received word that C-SPAN 2 "Book TV" will cover the FEE National Convention in Las Vegas, May 3–5. The network tentatively plans to tape interviews with six of our authors on Saturday:

Michael Ledeen, *Tocqueville on American Character*
Harry Browne, *How I Found Freedom in an Unfree World*
Mark Skousen, *The Making of Modern Economics*
Dinesh D'Souza, *What's So Great About America*
Charles Murray, *The Bell Curve*
Tom DiLorenzo, *The Real Lincoln*

"C-SPAN is very excited about our line-up of authors, " said Dr. Skousen, "and we are pleased that it will highlight FEE and Laissez Faire Books to a nationwide audience."

Dr. Skousen has also been invited to appear on "Book TV" sometime during the summer, to present his "Tour of the Bookstore" lecture.

"Book TV" airs on C-SPAN 2 each weekend from 8 a.m. Saturday to 8 a.m. Monday. For complete programming information, go to www.booktv.org.

We will also update the news through our www.FEEnews.org website.

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# IDEAS ON LIBERTY

May 2002 Vol. 52, No. 5


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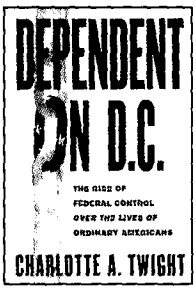



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FEE Home Page: www.fee.org

*President:* Mark Skousen

*Executive Director:* Stefan Spath

*Editor:* Sheldon Richman

*Managing Editor:* Beth A. Hoffman

*Editor Emeritus*
Paul L. Poirot

*Book Review Editor*
George C. Leef

*Editorial Assistant*
Mary Ann Murphy

*Columnists*
Charles W. Baird
Doug Bandow
Donald J. Boudreaux
Dwight R. Lee
Lawrence W. Reed
Russell Roberts
Thomas Szasz
Walter E. Williams

*Contributing Editors*

| | |
|---|---|
| Norman Barry | Wendy McElroy |
| Peter J. Boettke | Tibor R. Machan |
| Clarence B. Carson | Andrew P. Morriss |
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Cover photo by Keith Stanley (www.kestan.com).

PERSPECTIVE

## Setting Up Pigeons

The anti–free-market crowd is cackling over Enron. But who's really entitled to say, "I told you so"? Is this the result of unbridled robber barons? Or the predictable outcome of the regulatory regime?

There is only one sure consequence of pervasive regulation: a blunted wariness born of a false sense that government watchdogs are on the job. Regulators require corporations to make myriad disclosures and to be audited every year. Severe penalties are threatened for failure to comply. Under those circumstances, no potential investor could be as cautious about corporate wrongdoing as he would be if no such requirements existed.

But any regulation can be gotten around. Those without scruples or honor will always manage to spin their schemes. So we're left with something far worse than the socialist's nightmare: unbridled and unscrupulous businessmen *and* unwary investors, employees, and consumers.

Put bluntly, the regulatory environment indirectly sets up pigeons.

It can do so directly also, as *IOL* managing editor Beth Hoffman points out. Consider the "Chinese wall." The *New York Times* explained, "Wall Street firms are supposed to maintain a so-called Chinese wall to ensure that customers of their brokerage operations are not made privy to inside information gleaned by their investment bankers."

The law prohibiting that communication didn't work out so well in the Enron case. Discrepancies in the company's various statements could long go undetected because it is illegal for one department of a financial firm to compare notes with another.

The *Times* provides an example: Merrill Lynch, the underwriter for one of Enron's partnership offerings (called LJM2), "was aware of the off-balance-sheet figures for Enron. . . . But because the numbers were confidential, that information could not be shared with Merrill brokerage clients who were investing in Enron stock."



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The *Times* story continued: "In this case, securities experts said, *the intent of those laws was undermined*. The transactions '*followed the legal norms to produce a perverse result*,' said John C. Coffee Jr., a securities law expert at Columbia University. 'It's a case where the Chinese wall is working to injure public investors, rather than benefit them.'" (Emphasis added.)

Free-market advocates call such perverse results "unintended consequences." Protector became accomplice. Would Enron's investors (including its employees) have been worse off without such "protection"?

* * *

After September 11, pundits and politicians have been heralding the return of Big Government. When did it ever leave? Joseph Stromberg wants to know.

And speaking of Big Government, it got that way because it has devices to keep the people who foot the bill from detecting what's going on. In an excerpt from her important new book, *Dependent on D.C.*, Charlotte Twight describes the process.

The environmental movement and the regulations it has inspired are premised on the notion that human activity can harm the environment. Therein lies a monumental fallacy, Roy Cordato writes.

When the government of the District of Columbia bought private individuals' handguns and turned the guns into a sculpture, it did more than create bad art. William E. Pike has a review.

Enron would have hurt far fewer people had its charter warned that it might issue tainted audits and inaccurate balance sheets. Rather than new regulations, Fred Foldvary says, we need a clear codification of the market's rules.

People bemoan credentialism, but to Keith Wade, it's just the market's way of compensating for government's failure.

In the free market new technologies begin expensive but quickly fall in price and spread throughout society. The exception is medical technology—because the market isn't free, Gary Pecquet writes.

If it's illegal to bribe a court witness, why does the government get away with it? As Joseph Fulda points out, for a moment, it almost didn't.

As the seedless green grape demonstrates, capitalism makes weak men strong. Daniel Hager connects the dots.

The farmer is an exalted figure whom virtually everyone would exempt from the market's gales, including some self-styled defenders of capitalism. Scott McPherson explores the curious exception.

Politicians have many ways to subvert social cooperation and destroy prosperity. But, writes Christopher Lingle, it's hard to top populism.

Personal computers and the Internet seem to pervade American society and are becoming more common all the time. Yet some lament the "digital divide." Larry Schweikart examines the matter.

Confusion over the term "liberal" continues. So Jim Peron consulted two old books that should have cleared things up.

Why the perennial worry over a general falling of prices ("deflation")? Christopher Mayer seeks an answer.

Our columnists have another set of treats this month: Mark Skousen explores the right to be left alone. Lawrence Reed reports on a reason for optimism in Kenya. Doug Bandow warns against broadening the war against terrorism. Thomas Szasz sees resemblances between maternity and mental hospitals. Dwight Lee ponders the public interest. Donald Boudreaux recycles. Charles Baird finds the secret of success for public-sector unions. And Thomas DiLorenzo, encountering the claim that Enron and Argentina constitute market failures, replies, "It Just Ain't So!"

The lineup of book reviews is equally provocative, with these themes: software without copyright, the history of business, the Clinton-Reno Justice Department, the role of economics in politics, and the moral effect of wealth.

—SHELDON RICHMAN



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From The President's Desk

by Mark Skousen

IDEAS ON LIBERTY
MAY 2002

# The Right to Be Left Alone

"The makers of the Constitution conferred the most comprehensive of rights and the right most valued by all civilized men—the right to be let alone."
—JUSTICE LOUIS D. BRANDEIS

According to Thomas Jefferson and the Declaration of Independence, one of the "repeated injuries and usurpations" committed against the American people by the King of England was the erecting of "a multitude of New Offices, and . . . swarms of Officers to harass our people, and eat out their substance."

Today, following the tragic events of September 11, 2001, the American people face another troublesome threat—swarms of security agents harassing us at airports, borders, buildings, and highways. Like many of you who travel frequently, my wife, Jo Ann, and I have been subjected to these often overzealous security guards who ask inane questions; force us to remove our shoes, jackets, and belt buckles; and meticulously go through our carry-on bags. I've had my fingernail clippers confiscated twice. Jo Ann was frisked three times in one day. Others have fared far worse. My friend and *IOL* fellow columnist Walter Williams was almost arrested in Jacksonville, Florida, after he refused to be patted down. A congressman was required to disrobe. After these security encounters, I always feel my privacy, indeed my dignity, has been violated.

*Mark Skousen (mskousen@fee.org) is president of FEE. His website is www.mskousen.com.*

President George W. Bush has urged citizens to return to normal life, but business and domestic affairs are never the same when a war is on, and this war on terrorism is no exception.[1] Bush's proposed federal budget jumped 9 percent from last year, pushing the United States into a deficit again. Private enterprise has been forced to spend billions on security measures, a real burden on a recessionary economy. (Imagine, intelligent employees spending the rest of their lives trying to catch some nut out there, representing 1/1000 of 1 percent of travelers.) Airport security has now become federalized. And we have become, in the words of Sheldon Richman, "tethered citizens."

In revolutionary times, colonists were so incensed by the invasions of privacy and other personal abuses by British officers that Congress's first act was to pass a Bill of Rights, including Amendment III, "No Soldier shall, in time of peace be quartered in any house, without the consent of the Owner, nor in time of war, but in a manner to be prescribed by law," and Amendment IV, "The right of the people to be secure in their persons, houses, papers, and effects, against unreasonable searches and seizures, shall not be violated, and no Warrants shall issue, but upon probable cause, supported



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by Oath or affirmation, and particularly describing the place to be searched, and the persons or things to be seized."

The Fourth Amendment forms the basis of a "right to privacy," the right to be left alone, as Justice Louis Brandeis put it. The enjoyment of financial and personal privacy is fundamental to a free and civil society. True liberty is to be able to walk down the street, cash a check, buy goods, talk on the telephone, or take a trip without being hassled, hounded, followed, or interrogated by government agents. People should be able to get away from the madding crowds without being followed or asked stupid questions. When I travel abroad, there is no better feeling than walking through the green customs door marked "Nothing to Declare." When I return home and close the door, there is a feeling of security, knowing that the police aren't going to break it down in the middle of the night for a "warrantless" search. It happened in Soviet Russia and Nazi Germany, but surely not in America!

## Privacy Eroding

Yet the right to privacy so cherished by Americans of generations past is gradually eroding. New airport-security laws require all travelers to carry a "government-issued" ID, usually a driver's license or passport. Thus we have come dangerously close to creating a national identity card for all Americans. The war on drugs has made it virtually impossible to deal legally in large amounts of cash, the most anonymous form of doing business. Some banks are requiring thumbprints for identification. Mandatory drug-testing of students and employees is becoming commonplace without any reference to the constitutional principle of "probable cause." Since September 11, police routinely check automobiles and trucks coming into New York City without a warrant. Tampa and other big cities are videotaping citizens in "crime-prone" areas around the clock. California and other states are capturing all drivers on film and issuing tickets for alleged speeders.

I wrote the first book on financial privacy in the early 1980s.[2] It was a huge underground hit, selling over 400,000 copies. Clearly, vulnerable Americans felt the need for protection against potential lawsuits, government surveillance, prying relatives, aggressive salesmen, and professional thieves. From time to time, I am asked to do an updated edition, but I have refused. Why? Because the law has changed and become so complex that it takes a full-time professional to stay up on all the dos and don'ts. However, I can recommend an excellent newsletter that focuses on privacy issues: *The Financial Privacy Report,* published and written by Michael Ketcher (to subscribe, call 1-866-429-6681; P.O. Box 1277, Burnsville, MN 55337).

Despite the recent intrusions into individual personal affairs, you can still maintain a certain degree of privacy. You can take a car, bus, or train, and go to most destinations without being noticed or tracked. In small transactions, you can still pay with cash instead of using credit cards or checks. You can buy a large number of gold and silver coins with cash and avoid reporting requirements. You can refuse to give your Social Security number to schools, hospitals, dentist and doctor offices, insurance companies, and most private organizations (but not banks, brokers, or the IRS). You can open a foreign bank account with less than $10,000 and not have to report it. You can use a post office box to keep direct mail promoters from contacting you. You can demand a search warrant before allowing the police to come into your house or business, or to search your automobile.

In short, by maintaining a low profile, you can usually avoid the scrutiny of overzealous bureaucrats, nosy neighbors, or jealous relatives. □

1. Historian Robert Higgs makes this very clear in his excellent article, "How War Makes Government Bigger," *Ideas on Liberty,* December 2001.

2. Mark Skousen, *The Complete Guide to Financial Privacy* (Alexandria House Books, 1979; New York: Simon & Schuster, 1983).



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## Enron and Argentina Are Examples of Market Failure?

# It Just Ain't So!

In the eyes of *New York Times* columnist Paul Krugman, nearly everything that goes wrong in the world is caused by the fact that government is not big and powerful enough. In a mid-December 2001 column he blamed both the bankruptcy of Enron and the collapse of the Argentine economy on deregulation. But, as is so often the case with Krugman, the facts point in the opposite direction.

He claims that the Enron bankruptcy was all "about doing away with regulation" of energy prices and of financial trading. Huh? The regulatory budgets of both the Security and Exchange Commission (SEC) and the Commodity Futures Trading Commission (CFTC) are at all-time highs, and they employ more regulatory bureaucrats than ever. If anything, the Enron debacle proves once again the *ineffectiveness* of SEC and CFTC regulation. Enron collapsed *despite* layers and layers of financial regulation.

Krugman's claim that Enron used its "political clout" to create a "regulatory black hole" in energy markets is equally absurd. There has been very little, if any, deregulation of energy markets: oil, electric power, and natural gas remain among the most heavily regulated industries in the United States, as they have been for over a century. Radical environmentalists in and outside government continue to impose a regulatory blockade on energy development. What Krugman calls "deregulation" is really re-regulation, or a change in the form of regulation. A good example is California's crazy electric power regulatory regime that blocks energy development while placing price controls on power, thereby guaranteeing periodic shortages and blackouts. He routinely misleads his readers by referring to this Byzantine regulatory morass as "deregulation."

Like other anti–free-market commentators, Krugman also spreads the false tale that Enron's chairman, Ken Lay, was a free-market disciple. This too is, well, baloney. Lay was a member of the group of extreme anti-capitalist ideologues known as the Union of Concerned Scientists. He was also a strong supporter of the Kyoto global-warming treaty. He supported this treaty (which the Bush administration refused to sign on to), because he wanted his company to profit from another Byzantine regulatory scheme concocted by the government: the trading of carbon dioxide emission permits. Lay wanted government-imposed restrictions on carbon dioxide emissions to create an artificial market for air pollution "credits" to be purchased to burn coal. A government-controlled and -supervised "market" is not a genuine market, of course, but more like the failed experiments in "market socialism" that occurred in some of the former communist countries.

Enron collapsed primarily because it made some bad business decisions. It reportedly invested billions in failed power plant, utility, pipeline, and waterworks companies in India, Brazil, and Great Britain. When the profits from these investments failed to materialize, investors got wise and dumped Enron stock. The energy-trading business is competitive and, as with all competitive industries, market leaders can expect their profits to be whittled away by new competitors.

If there was accounting fraud, that's not a result of "deregulation" but the fact that there are sinners in all walks of life. Governments commit accounting fraud all the time; during the Clinton administration it was reported by Gene Epstein of *Barron's* that the Social Security and Federal Highway



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Trust Funds were being plundered and the money placed into the current-year budget so that Clinton and Congress could take credit for balancing the budget. But don't expect Krugman ever to call for smaller government whenever such fraud is uncovered.

In this respect Enron's demise is an example of free-market *success*. The energy trading market in general is thriving; the fact that one firm that once had 25 percent of that market has left the industry is by no means an example of "market failure."

## Wrong on Argentina Too

Krugman is just as wrongheaded in his comments on Argentina. He blames the entire collapse of the Argentine economy on one thing: that country's adoption of currency boards, as have been advocated by such free-market economists as Steve Hanke of Johns Hopkins University. Once again Krugman commits the post-hoc-ergo-propter-hoc fallacy (after this, therefore because of this). Yes, a currency board existed in Argentina, and yes, its economy has gone down the tubes. But Krugman never even attempts to prove causation. Anything that smells like a free-market institution must, in Krugman's mind, be the culprit.

In reality, the fault lies with the International Monetary Fund (IMF) and the U.S. government, which have been subsidizing Argentina's failed statist economic policies for many decades. The IMF promised to subsidize Argentina's currency-board regime, which caused a flood of investment in Argentine bonds. The Argentine government was known to be hopelessly spendthrift and corrupt, but with the IMF's guarantee, international investors began earning above-average returns on Argentine bonds with what they saw as virtually no risk. IMF funding created a massive moral-hazard problem.

The Argentine government used this massive influx of credit to enlarge an already bloated government sector, which always causes the private sector to shrink. Government spending doubled during the decade of the 1990s, far outstripping personal income growth. When a recession hit in the mid-1990s, the government responded in a prototypical Keynesian way by spending even more extravagantly and accumulating more debt. Private investors began shying away from Argentine bonds in 2000, at which time the IMF poured another $48 billion down the government rat hole.

The one good thing the IMF did finally was to refuse to continue to bail out Argentina's politicians, and that is what caused the bottom to fall out of the Argentine economy.

For decades, Argentina has practiced the kind of economic statism that is championed by the likes of Paul Krugman. Its guiding philosophy has been that its economy should be centrally planned by domestic government elites with the help of the IMF bureaucracy. Its politicians were shielded from taking responsibility for the inevitable failures of these policies by IMF and U.S. government foreign aid. Now that the Argentine bubble of economic statism has burst, the Paul Krugmans of the world are frantically seeking to shift the blame to the free market. Sorry, Professor Krugman, it just ain't so.

—Thomas J. DiLorenzo
(TDilo@aol.com)
Department of Economics
Loyola College, Maryland



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# The "Return" of Activist Government?

*by Joseph Stromberg*

In the *New York Times* of December 13, 2001, John D. Donahue joins the crowd that is presently arguing—or hoping—that the events of September 11, 2001, have cleared a path for the "revival" of big, all-knowing government. I do not wish to argue, here, why that might be undesirable. I do contest Donahue's historical construction of the question.

As I have pointed out elsewhere,* the whole claim that "government is back, hooray, hooray" supposes that at some point in living memory government actually receded to a detectably appreciable degree. Let us see how Mr. Donahue has mapped the terrain.

He first sets up his straw man. Evidently, Americans have been infatuated with markets and "market solutions" and have developed a whole "mythology" around that infatuation. But now things are changing, and "[a]fter fifty years of market ascendancy," government may be about to "reclaim its role as an integral and admirable part of American life."

Before one can say "Not so fast!"—he's off. Security at airports "has been wrenched from the market and entrusted to government." Polls show greater "trust in the presidency, federal agencies, even Congress." President Bush may be turning from budgetary cheese-paring and "massive tax cuts" to big spending. (Parenthetically, the "liberal" notion of what a massive tax cut consists of never ceases to amaze.) Evidence even exists that young people are once again looking favorably on government "service." This libel on the younger generation should not go unrebuked, but that is a matter for another time.

This happy "rebound" of government may overcome the negative politics of Reagan, Bush I, Clinton, and Dubya, all of whom indulged themselves, rhetorically, in taking potshots at omnicompetent government. Now we come to the heart of Mr. Donahue's causal-historical viewpoint. During the years he is so keen to discredit, "markets seemed infallible" and went from success to success. At the same time, Americans' "wariness toward authority" grew into "cynicism about the competence of our public institutions." In other words, people came to see that markets gave them what they wanted, while the state did not. Donahue concedes that changing perceptions rested on "no capricious shift." Yet he still laments people's lack of belief that government could "define and pursue shared goals" for society.

But fortunately, Donahue says, government's dry spell is (or may be) behind us.

It is odd that *there is no mention of the present "war"—or past mobilizations*—as a causal factor for any of the trends that so uplift Mr. Donahue's spirit.

*Joseph Stromberg (stromberg@mises.org) is the JoAnn B. Rothbard Historian in Residence at the Ludwig von Mises Institute.*

*See "Big Government, Having Never Gone Away, Is Now Said To Be 'Back,'" www.antiwar.com/stromberg/s092801.html.



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Let us try to sort these things out. In the first decades of U.S. political history we see a fierce struggle between a program of American mercantilism and its opponents. No one disbelieved in markets as such, but there was plenty of room for conflict between those who argued that subsidies to industry, tariffs, and the like were the very essence of a properly organized market economy and those who held a laissez-faire view of the political economy.

It was the Secession War that first decisively ratcheted up the level of government activity. After the war the level receded until the next war, which coincided with Populist and Progressive demands for reform via a more powerful federal government. Progressive reform reached its high point during World War I. The Great Depression—never "cured" by the New Deal—gave way to World War II. In this period of state-building a much higher "normal" level of federal activity took hold.

In a real sense, the wars provided the key to state growth; the domestic reform programs were parasitic on the states' role in wartime. The books of Bruce Porter, Robert Higgs, and Martin Van Creveld are revealing in this connection. Conservatives turn a blind eye to the war-reform linkage because they tend to take the wars at face value while objecting to the reforms. Modern liberals often glory in the connection. Hence all the Greatest Generation hype of late.

## Busy Government

It is easy for Donahue to say that government was "weak" for 50 years, if the benchmark is the capacity of government to tax, conscript, seize, and confiscate that it enjoyed during World War II. But since, as Professor Higgs has shown in various articles, Cold War levels of military spending were somewhere in between normal peacetime levels and the level of World War II, there was quite a lot that government was in fact doing during those 50 years that Donahue sees as a civil servant's nightmare.

Further, in the Cold War atmosphere of sustained "emergency"—to which no end was foreseen—all manner of interventions into economy and society gained a hearing, which otherwise might never have taken hold or would have been debated on their merits. Instead, they could be presented as essential to "winning" the Cold War. Among these might be numbered: the interstate highway system, coercive racial integration, state-subsidized nuclear power, and this is the barest beginning.

By the late 1940s there began a revival of classical-liberal ideas, symbolized by the wide readership found for F. A. Hayek's *Road to Serfdom* (1944). Over those 50 years that seem "lost" to Donahue, much progress was made for classical liberalism in the war of ideas.

Knowledge of the workings of markets was, after all, abroad in the land in the days of Jimmy Carter, but such knowledge did not prevent, or even slow, creation of a whole useless cabinet-level bureaucracy. This was the Department of Energy, which is still with us despite the evaporation of its proximate cause or excuse, the international oil cartel, OPEC, whose evaporation was predicted by all sensible economists at the time of the department's founding.

While Carter had only promised to preside over pragmatic reductions of government activity in some areas, Ronald Reagan came in breathing the rhetoric of so-called "neoliberalism," that is, the standard rhetoric of American conservatism at that time. At this late date, I hope that no one actually believes that there was a Reagan Revolution that reduced the federal government to some shadow of its former self.

And so it went, down toward the present. The medical reform proposal (Hillary Care) went down, not because of wide respect for free-market ideas, but because the partisan politicians could not agree on the details of who would get what out of this huge potential barrel of pork.

As for Americans' cynicism about government, this was well-earned, as each new reform worsened its services—public schools, for example. It is hard to think of government as "back." It never went away. On the other hand, we should all fear a further upward turn of the ratchet. □



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# Designing Dependence

*by Charlotte A. Twight*

Government now permeates American life, shaping and determining in countless ways the choices available to us. As Tocqueville feared, the U.S. government has largely succeeded in its efforts to spare us "all the care of thinking and all the trouble of living." Through Social Security, Medicare, public education, and the rest, the sphere of autonomous individual action grows ever smaller, despite widespread understanding that personal responsibility is essential to self-respect and therefore necessary to individuals' pursuit of happiness. In the modern redistributive state, we are no longer free to choose in many fundamental areas of our lives.

How has it happened? What are the specific mechanisms by which Americans have been induced to relinquish their patrimony of liberty—the ways in which they have been, in Tocqueville's prescient words, "softened, bent, and guided" to government purposes? This book develops a new framework for understanding the political techniques and institutional mechanisms that have led us to embrace pervasive government controls and corresponding personal dependence. Deliberate manipulation of political transaction costs—meaning costs to individuals of reaching and enforcing collective agreements regarding the role and scope of government—will be seen as central to this process of softening, bending, and guiding the populace to government purposes.*

Conventional wisdom often views dependence on government in America as an inadvertent byproduct of benign legislative intent, codified in democratically adopted measures reflecting the will of the people. To the contrary, this book shows that manipulating costs of political decision making in order to achieve results initially *inconsistent* with actual public preferences has been a recurrent strategy in capturing and maintaining increased government authority over U.S. citizens. The key insight is that political transaction costs shape action and inaction in political contexts, and that those transaction costs routinely are manipulated by self-interested political actors. In contrast to some economists' visions of a transaction-cost minimizing state, this book documents government officials' characteristic willingness and ability to deliberately increase the political transaction costs facing others on issues that influence the scope of government authority.

How has the federal government been able to so greatly expand its powers, sometimes in ways initially contravening public sentiment, without provoking rebellion? My

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*Charlotte Twight is a professor of economics at Boise State University. From the book* Dependent on D.C. *by Charlotte A. Twight. Copyright © 2002 by Charlotte A. Twight. Reprinted by arrangement with Palgrave, LLC, New York, N.Y.*

*Editor's Note: For more details on this process, see Charlotte Twight, "A Constitutional Counterrevolution," *Ideas on Liberty*, October 2000, p. 21.



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*But politicians do more than lie to secure passage of legislation they favor: they also seek to increase other costs to individuals of taking political action. One striking example . . . is the Supreme Court's role throughout the twentieth century in changing the Constitution, sidestepping the constitutional amendment process designed by the Framers.*

answer, developed at length in subsequent chapters, is that government officials have both the power and the personal incentives to change the costs to private citizens (and to others in government) of taking particular political actions. Through statutory law and otherwise, they change the rules of the game in diverse ways that alter the costs of resisting particular political measures. In the language of economics, government officials change the transaction costs to individuals of taking political action on measures that influence the scope of government authority. They do so through familiar political behavior such as lying and misrepresentation—which raise the costs of obtaining accurate information—and also by changing in other ways the costs to private individuals of achieving and enforcing political agreement on matters that determine the scope of government authority. I provide many examples of this behavior in subsequent chapters.

For government officials, the trick is to selectively curtail political resistance. In each of the policy areas examined in this book, deliberate government manipulation of political transaction costs will be shown to have achieved exactly that result. Government officials shaped political outcomes to their own liking in these cases by deliberately increasing the costs to private citizens of resistance. Once established, the new institutions refashioned the status quo into one characterized by greater government authority over people's lives. In turn, such institutional change facilitated widespread ideological change that buttressed and reinforced the new powers of government.

It has been understood for centuries that politicians lie, of course. Niccolò Machiavelli, giving advice to his prince in 1513, described forms of calculated political decision making echoed by the Clinton administration from 1993 to 2000. Lying about the nature and consequences of proposals to expand federal authority is clearly one way of raising the costs to individuals of resisting them.

But politicians do more than lie to secure passage of legislation they favor: they also seek to increase other costs to individuals of taking political action. One striking example . . . is the Supreme Court's role throughout the twentieth century in changing the Constitution, sidestepping the constitutional amendment process designed by the Framers. The amendment process purposely made it costly to change the scope of government authority established by the U.S. Constitution. Actions by Supreme Court judges that supplanted the constitutional amendment process—for example, judicially expanding the Constitution's interstate commerce power—both increased the costs to citizens of maintaining the established scope of government and reduced the costs to government officials of vastly expanding the scope of federal authority over the economy. . . .

My concern in this book is not only the growth of dependence but also the growth of an ideology of dependence—the normative judgment that broad governmental power creating pervasive dependence on government is desirable. Accordingly, I identify linkages connecting government manipulation of politically relevant transaction costs,



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dependence on government, and the emergence of ideological change. I argue that the continued experience of dependence on government over time fosters acceptance of the propriety of such dependence, making it increasingly difficult for society to envision politico-economic solutions based on individual autonomy.

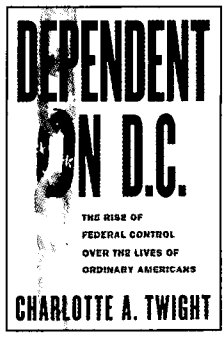
Consider again the transformations wrought in America in the twentieth century. How could the politico-economic landscape have been so altered? Why does the peacetime public now acquiesce to the forced turnover of more than 33 percent of U.S. citizens' total annual income to governments and the billions of uncompensated labor hours spent creating records to satisfy these governments? What has made possible the "gentle" servitude, the "enervating" of people's independence that Tocqueville so clearly foresaw? My thesis is that political transaction-cost manipulation was practiced both at the inception of the new governmental institutions and as an integral part of their subsequent implementation, maintenance, and growth. Buttressed by this transaction-cost augmentation, processes of ideological change then reinforced the institutional changes and made them self-perpetuating.

While "manipulation of political transaction costs" at first may seem dry and theoretical to some readers, it will quickly become clear that governments have put the concept into actual practice in ways that are all too real, using it as a central tactical strategy to expand their power. If we wish to preserve our freedom, we'd better come to understand it. After all, federal officials already do. With it, the central government has steadily encroached upon our once private lives. □


# Dependent on D.C.

## The Rise of Federal Control Over the Lives of Ordinary Americans

***By Charlotte Twight***




"If the Framers of our Constitution were alive today, they would be shocked by the loss of so many liberties they sought to guarantee for us. Professor Charlotte Twight has produced an excellent analysis of the how and why of the diminution of our liberties. She shows that today's intrusive federal government, unthinkable to the Founders, is not some evil conspiracy but the natural result of Americans attempting to live at the expense of one another. The plain language of *Dependent on D.C.* and its thorough diagnosis not only puts us on alert, it might even suggest some strategies to strike at the menace of runaway government."
—Walter E. Williams, John M. Olin Distinguished Professor of Economics, George Mason University, Fairfax, Virginia.

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IDEAS ON LIBERTY
MAY 2002

# A Leonard Read for Africa?

A candle has been lit in east Africa. It shows promise of spreading much light where there is now much darkness. In time it may grow to illuminate an entire continent. Its appearance is a testimony to perseverance and the power of ideas, as well as a tribute to this very publication. The candle is in the form of east Africa's first free-market research and educational organization, or "think tank," and the man who lit it is one remarkable 31-year-old Kenyan named James Shikwati.

Kenya, you must understand, is not a place that is known for free markets or free-market ideas. It is hardly a hospitable place for an organization devoted to these things to emerge, though the description of the country from the *2000 Index of Economic Freedom* (produced by the Heritage Foundation and the *Wall Street Journal*) surely indicates a crying need for them. Rating Kenya as "Mostly Unfree," the *Index* laments that in spite of recent reforms, "the privatization program and civil service reduction efforts have stalled, the government continues to dominate many key industries, the infrastructure continues to deteriorate, political corruption remains rampant, and the rule of law is weak."

As a young man growing up in the remote Rift Valley of western Kenya, James Shikwati heard little or nothing about free-market ideas. But early on he exhibited traits that others increasingly recognized as signs of leadership and determination. His brother Charles recalls an incident when he and James were teenagers and the latter signed up for the local high school track team. Slight of build and no match for the more seasoned athletes, James was passed by all the runners as hundreds of spectators looked on. "He did not drop out as expected of someone so far behind," says Charles. "He stayed in the race and ran so hard that he became the center of attention. Instead of cheering the runners that were so far ahead, the crowd started cheering James. He stole the show."

As an undergraduate student at the University of Nairobi in the early 1990s, James developed a strong intellectual curiosity and a keen appreciation for philosophy. He formed and chaired a lively student philosophical association and attracted the attention of a noted professor, Clement Oniang'o, then the dean of the department of social sciences. Oniang'o encouraged James to pursue further studies outside Kenya and while seeking information about scholarships, James acquired a copy of a little book with a mesmerizing message. It was Frédéric Bastiat's *The Law,* published by FEE.

Moved by Bastiat's rigorous logic, and sensing that it could have powerful impact in statist Kenya, James wrote to FEE and secured a subscription to this magazine. Something about a particular column of mine on education prompted him to write his first of many letters to me in 1997—commencing a nearly five-year correspondence. Ever since, James has devoured every maga-

*Lawrence Reed (Reed@mackinac.org) is president of the Mackinac Center for Public Policy (www.mackinac.org), a free-market research and educational organization in Midland, Michigan.*



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zine, journal, and book on freedom ideas that he's been able to get his hands on, and both FEE and I have been happy to send them by the dozens.

James put his growing command of freedom ideas to work in the classroom from 1996 until early 2001 at Kiptewit High School, where he taught courses in geography and ethics. A fellow teacher whom he came to influence greatly, Tom Majanga, says that "Most of his colleagues on the faculty shuddered whenever James declared he was a capitalist. He would defend self-interest as a virtue." Such controversial views expressed in a public school landed James in hot water. School officials first arranged for his eviction from his apartment on trumped-up charges, and then threatened to fire him. That's when I received a watershed letter from James 18 months ago, informing me that with his wife's approval, he was going to quit teaching, move to the capital, Nairobi, and start east Africa's first free-market research and educational institute. In the middle of 2001, the Inter-Region Economic Network (IREN) was born.

## First Anniversary

Operating on a financial shoestring, out of a modest apartment with a computer and not much else, James is about to mark his first anniversary as head of IREN. His payroll is a one-man show for now, but a growing number of inspired volunteers provide in-kind assistance in the form of accounting, phone-answering, legal, and other help. That gives James time to make the rounds, getting to important people in the media and government. He writes well and has had amazing success in getting Kenya's largest newspapers to publish his incisive commentaries applying free-market prescriptions to the country's problems. He has a website at www.irenkenya.org.

I visited Kenya this past January to meet James for the first time. He's everything all of us who have been helping him were hoping for—charismatic, dedicated, dogged, articulate. He's a consummate networker, never missing an opportunity to make an acquaintance and introduce freedom ideas. Like FEE's founder, Leonard Read, James's approach is gentle but compelling. He does not harangue; he persuades through a combination of friendly Socratic inquiry, an appeal to fundamental principles, and unassailable logic. An influential journalist touched by James's appeal, Bob Wekesa of the *East African Standard*, admires his tenacity and considers the young Kenyan "an inquisitive, new-generation thinker who is bringing people to a new understanding of the value of free enterprise."

When nearly 50 people showed up to hear two lectures James had arranged for me to deliver, I saw firsthand the good work he has already done. I've rarely spoken to people more enthusiastic about freedom. Many of them gushed about the young man who had opened their eyes and made them think for the first time about east Africa's enormous potential as a free society.

On IREN's agenda for this year are the translation into Kiswahili of Ken Schoolland's superb book, *The Adventures of Jonathan Gullible: A Free-Market Odyssey*; public lectures at universities in the Nairobi area; a stream of incisive commentary for the nation's newspapers; and a workshop and a study on how free-market environmentalism can promote wildlife conservation.

James Shikwati and IREN are proof positive that ideas can motivate and make a difference. The seeds of a brighter, freer east Africa are now being planted in Nairobi. In time, the work James has started may liberate millions. Where there was stagnation and despair, there is now good reason to have hope for Africa. □



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IDEAS ON LIBERTY
MAY 2002

# The Impossibility of Harming the Environment

*by Roy E. Cordato*

"The 'polluter pays principle' states that whoever is responsible for damage to the environment should bear the costs associated with it."
—United Nations Environmental Programme[1]

The "polluter pays principle" appeals to our sense of justice. People should be held responsible for their actions, and polluters who cause damage to others should "pay" for that damage. Furthermore, forcing polluters to bear the costs of their activities would enhance economic efficiency. In other words, appropriately applied, policies based on the principle face no trade-off between the efficient working of a capitalist system and environmental protection.

But as with most general principles, the devil is in the details. In this case the details relate to basic questions that any application must answer: How do we define pollution? Who is a polluter? How much should the payment be, and to whom should payment be made? The answers to these questions are at the heart of whether an application will be either just or economically efficient.

Most advocates of the principle never talk about harms to people. The statement above is typical. Polluters are those who "damage" or impose "costs" on the *environment*. This language is common. The U.N.'s "Rio Declaration on Environment and Development" states that "National authorities should endeavor to promote the internalization of environmental costs and the use of economic instruments. . . ."[2] (More on this below.) The "Draft International Covenant of Environment and Development" states: "Parties shall apply the principle that the costs of preventing, controlling, and reducing potential or actual harm to the environment are to be borne by the originator."[3]

Ultimately terms like "environmental costs" and "damage to the environment" can mean anything a policymaker wants them to mean. Since all human activity involves altering (damaging?) the natural environment, the "polluter pays principle" as defined by its most vocal advocates can be invoked to justify taxing or regulating any consumption or production activity, and often is. Indeed this may be the point of using such nebulous language.

Closely tied to that principle are policies typically referred to as "market based."[4] These policies are broken down into two categories, taxes and tradable permits. Both are seen as attempts to "make the polluter

*Roy Cordato is vice president for research and resident scholar at the John Locke Foundation. His more extensive discussion of the "polluter pays principle" can be found at www.iret.org.*



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pay" by attaching a fee to the polluting activities.

The taxation approach is most direct. The tax would be paid either in the form of an emissions fee or an excise tax on the product associated with pollution. The tradable-permits approach (also called cap and trade) would first have the government establish an overall acceptable level of pollution for an industry and would then distribute emission permits to firms in that industry. The total amount of emissions represented by these permits would add up to the overall level that was initially established. Companies could then buy and sell these permits based on their needs to emit the pollutant and their abilities to find pollution-abatement techniques. The point is that in either case, the polluters are made to "pay" for their polluting activities, either through a tax or through the purchase of permits from others in the industry.

While the moral case for market-based instruments is generally centered on the concept of making the polluter pay, the economic justification is based on the idea that using market-based incentives to accomplish environmental goals is more efficient than traditional command-and-control policies. Theoretically, polluters who must pay will have to consider all of the costs associated with their production activities and use resources more efficiently. Furthermore, they will have an incentive to find the lowest-cost methods for reducing emissions.

## Manipulated Definition

The problem is that, in advocacy and practice, the supporters of market-based instruments, like the supporters of the "polluter pays principle" more generally, manipulate the definition of cost to make it consistent with the vague concept of harm or damage discussed above. Economics attaches the concept of costs to human beings and individual decision-making. "Cost" refers to what must be given up when a person chooses one course of action rather than another, or when someone else's activities prevent a person from choosing a course of action. For example, in the case of a company's polluting a river, the cost might be to downstream recreational users who have to give up or cut back on certain activities that the pollution is preventing them from pursuing. From this perspective then, pollution problems arise because the polluter is imposing costs on other human beings. It is human users of the river who bear the costs, not the river itself.

As with the "polluter pays principle" more generally, many advocates of market-based instruments misuse the economic theory by redefining the concept of costs and damage to apply to things rather than to people. But the environment does not incur costs. Only people do.

An article by David Pearce and Kerry Turner is typical. In the name of "making the polluter pay," the authors call for excise taxes on the use of beverage containers. Their claim is that "*environmental damages* from packaging waste is not reflected in the prices of packaged products" and that "the size of the levy needs to be related directly to the *environmental damage* done by the production and consumption of the packaging, or to the costs of *restoration to the environment*" (emphasis added).[5] Nowhere is there a reference to costs or damage to actual people from the use or disposal of beverage containers. Unfortunately, such abuse of the concept of costs is not discouraged among economists. This article appeared in a respected and refereed academic journal.

The notion that polluters should be made to pay for the damage they cause is nothing more than an extension of the idea that people should be held accountable for their actions. This fundamental principle is made coherent by property rights. When person A does harm to person B, it is understood that A has done damage to B's person or property. The appeal of a "polluter pays principle" is that A makes B whole again; that is, to the extent possible, he provides restitution, most likely in the form of monetary compensation, for B's suffering.

It is right that environmental policy should make the polluter pay so long as it is grounded in these basic principles. Within this context ambiguity is greatly reduced about what



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kinds of emissions or by-products of production processes should be characterized as pollution, who should be identified as a polluter, and what the polluter should pay and to whom. If a producer emits a substance, whether into the air, a body of water, or the ground, and those emissions cause health problems or cause damage to people's property, then those emissions would be correctly characterized as pollution and the company as a polluter. The payments that the company would be forced to make should go, not to the government in the form of a tax or to other companies to buy permission to pollute, but to those in the community who have suffered from pollution.

From this perspective pollution problems are the result of conflicts over the use of a resource. Persons A and B would both like to use the same resource for conflicting purposes. Usually the presence of private property allows for such conflicts to be resolved both peacefully and in a mutually beneficial way, even when the issue involves the environment. For example, on wildlife preserves owned by the Audubon Society it is not uncommon to see oil companies drilling for crude. While the Audubon Society and oil companies may want to use this land for what might first appear to be conflicting purposes, private ownership provides a strong incentive for the parties to compromise and resolve the differences. By leasing part of its land for oil exploration, the Audubon Society can gain revenues to purchase other lands while insuring that the drilling takes place in an environmentally friendly way. This is not the case on "publicly" owned lands, such as the Alaskan National Wildlife Reserve (ANWR), where any drilling is viewed as being at the expense of environmental concerns.

## Use Without Permission

In cases where someone decides to make use of another's property without permission, the problem is resolved by applying the simple rule that the person who owns (has title to) the property is the one whose purposes prevail. This approach takes the focus off the physical environment, per se, and places it on human beings and their right to live their lives unmolested. An activity is polluting only if it harms others.

This approach to the "polluter pays principle" has two distinct and mutually reinforcing advantages. First it is consistent with the principles of liberty. Under a property-rights–grounded principle, people are free to pursue whatever production or consumption goals they desire so long as there is personal accountability for any and all damage to others or their property. Second, if generally invoked as a guiding principle of environmental policy, it will enhance economic efficiency and social welfare. Moreover, those involved in production activities will attempt to ameliorate problems before they occur. There would be a strong incentive to develop new technologies that eliminate or minimize pollution from the outset.

Environmental problems tend to arise when people are allowed to impose costs on others by degrading other people's property or by using property that is unowned. A property-rights-based "polluter pays principle" would go a long way toward solving many of these problems, first by seeing to it that existing property rights are enforced and by providing principled guidance for the privatization of currently unowned resources by courts and legislatures. It will be much easier for lawmakers and adjudicators of disputes to move in the right direction once the target is clearly identified. □

1. United Nations Environmental Programme, *Taking Action*, Chapter 2, p. 3.
2. "Rio Declaration on Environment and Development," Principle 16, The U.N. Environment Programme, found at www.unep.org/documents/default.asp?DocumentID=78&ArticleID=1163.
3. "Draft International Covenant on Environment and Development," Article 11.6, World Conservation Union, found at www.iucn.org/themes/law/the_draft_covenant.html.
4. For the distinction between market-based environmentalism and free-market environmentalism, see Roy Cordato, "Market Based Environmentalism and the Free Market: They're Not the Same" *The Independent Review*, Winter 1997.
5. David Pearce and R. Kerry Turner, "Packaging Waste and the Polluter Pays Principle: A Taxation Solution," *Journal of Environmental Management and Planning*, Vol. 35, No. 1, 1992, p. 6.



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IDEAS ON LIBERTY
MAY 2002

# Taxes into Plowshares

*by William E. Pike*

Yet another monument to state control has been erected in Washington, D.C. No, not the Franklin D. Roosevelt Memorial. In this case, the monument is a lesser-known sculpture called "Guns into Plowshares." This work, erected in 1997, stands in Judiciary Square close to the National Law Enforcement Officers Memorial. Dubbed a monument to peace, the sculpture is actually a monument to the anti–gun-rights lobby.

The work has its origin in a 1994 gun "buyback" program administered by the District of Columbia Police Department. Through this effort, the District purchased 3,000 privately owned handguns in the name of ending handgun violence. The question of what to do with all these guns was answered by artists Esther and Michael Augsburger, who suggested using them in a sculpture of a plow, playing on the well-known scriptural reference: "He will judge between the nations and will settle disputes for many peoples. They will beat their swords into plowshares and their spears into pruning hooks. Nation will not take up sword against nation, nor will they train for war anymore" (Isaiah 2:4).

The result was a four-ton, 16-feet high sculpture composed of steel and 3,000 disabled handguns, imitating a tremendous plow. Some might call it art, but others might call it instead the art of exploitation. The sculpture represents the fallacy of gun control and government intrusion at many levels.

First, the term "buyback" wrongly insinuates that the government has some primary right to all property to begin with, and that it was simply regaining possession of what originally belonged to it. In fact, it couldn't buy the guns *back* at all.

Second, the program was based on the oft-repeated fallacy that guns, and not criminals, commit crimes. Purchasing 3,000 handguns from citizens can do nothing to reduce crime. Criminals, obviously, will not sell their weapons to the police department. As for crimes of passion, which an otherwise law-abiding gun owner might commit, no one ever needed a gun to cause another harm. The logic behind a gun "buyback" also ignores the argument—and the evidence—that gun ownership protects many citizens and actually *reduces* crimes. (See John Lott's *More Guns, Less Crime.*)

Moreover, the law-abiding citizens who sold their guns were under the mistaken assumption that they would profit from the sale. However, they paid for their small profit in two ways. At some level they were taxed for the program. But even worse, they found themselves with slightly less freedom than before: the program represented one more lurch forward in big government's bid for control.

*William Pike (wpike_1@msn.com) is a graduate student at Duke Divinity School in Durham, North Carolina.*



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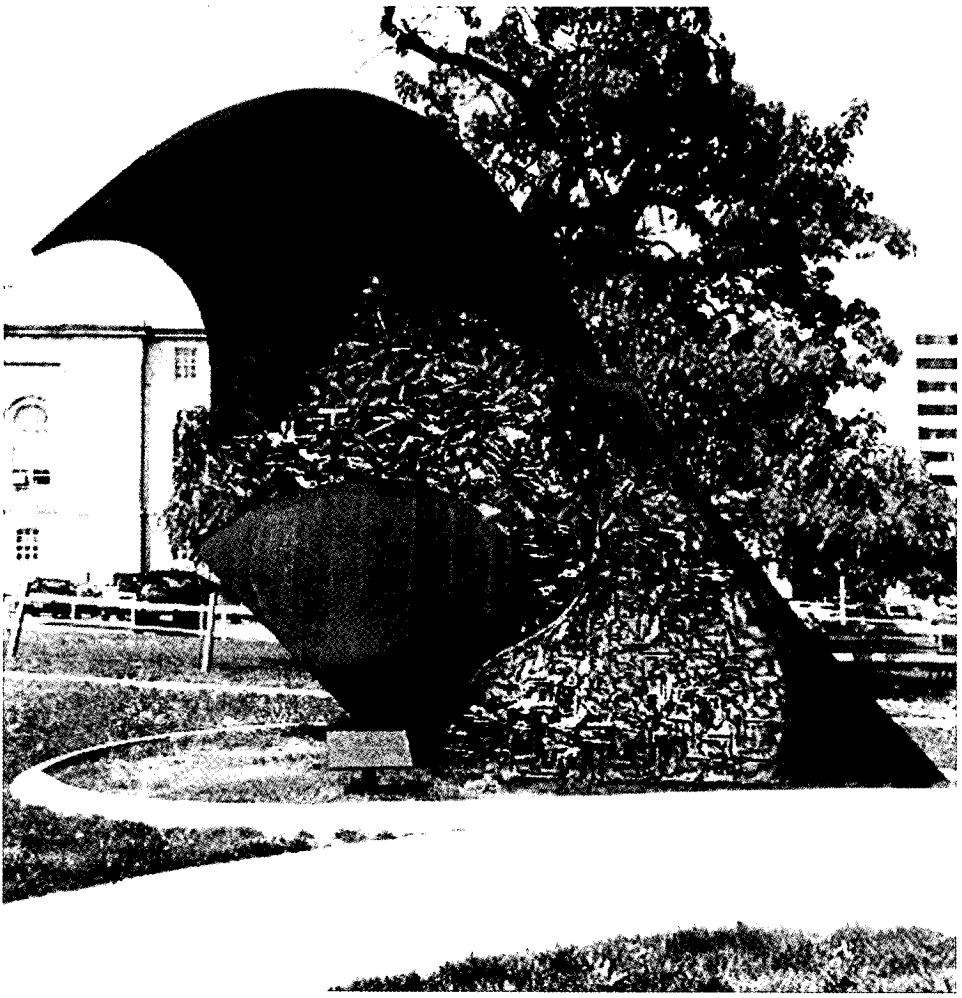

PHOTO BY KEITH STANLEY

*"Guns into Plowshares," Washington D.C.*

One can also find an interesting misuse of scripture in the very theme of the sculpture. The scripture being referenced refers to the peacefulness of nations, not the disarming of the populace. Those who believe in a powerful, coercive government should not celebrate such a government by quoting scripture about peace. Liberties are not stripped away by peaceful governments.

Finally, the very placement of the sculpture can be seen as insulting. Those who planned the sculpture felt that the work's proximity to the National Law Enforcement Officers Memorial would point out the role of handguns in violence against peace officers. On the contrary, the sculpture is a slap in the face to peace officers who serve with the intention of protecting citizens' rights. In this case, those who gave their lives that constitutional rights might be preserved are memorialized by one monument, while another nearby lauds the stripping of one of those rights from the citizens they died to protect.

Perhaps the saddest aspect of this monument is that so many citizens will pass by it in an attitude of awe and reverence, never realizing what it *truly* symbolizes. It is up to lovers of liberty to point out that in this case art has been used to commemorate the power of the state and the death of individual freedom. □



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IDEAS ON LIBERTY
MAY 2002

# Enron and the Law of the Market

*by Fred E. Foldvary*

People will learn lessons from the collapse of Enron. Some of these will be the wrong lessons.

Critics of markets claim that the Enron debacle shows how "capitalism" is defective and proclaim that the government should increase the regulation of corporations and financial markets. There does need to be a change in government policy, but not in the direction of greater interference with business.

A market needs to have clear rules about property rights, and this implies a general Law of the Market about telling the truth. What we need is a clearer codification of the Law of the Market, enforcement, and penalties against fraud. Fraud is a type of theft, and theft is a violation of market rules.

Let's start with the accounting firms that are supposed to audit corporations. The purpose of such audits is to ensure that the company has truthfully and fully accounted for its operations. This implies that the auditor should be impartial and not be swayed by any financial interest in the company.

That was not the case with Enron. Its auditing firm, Arthur Andersen, was also a consultant to Enron. In my judgment, that constituted a potential conflict of interest. If the auditor reported accounting problems, that might reduce its consulting income. Some argue that the government should prohibit auditing firms from also doing consulting work for the firm it audits. I argue for a noninterventionist policy.

The Law of the Market would require that all statements made by firms be truthful unless the company charter clearly and explicitly states that it might lie. The Law of the Market would also require that external audits of corporations be impartial, with firms having no financial interest in the company or any links other than the auditing, unless it is clearly and explicitly stated in the charter that it might have other business with the auditing firm, or that it might not be audited at all. It should be up to the shareholders to take on risks, but they should know what those risks are regarding company reports.

If the company's charter states that it may be audited by firms that also have other financial interests in the company, then all shareholders are warned that the audits might be suspect, and that the accounting reports—the balance sheet and income statements—might be misleading. The value of the shares will then be discounted to reflect this.

The Law of the Market would also specify that the accounting reports of a company fully show all assets and liabilities of the firm at current market prices, unless its charter states otherwise. Enron was able to hide liabilities in partnerships, which were not fully disclosed. A firm's business includes its

*Fred Foldvary (foldvary@pobox.com) teaches economics at Santa Clara University.*



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membership in partnerships, and if a firm wishes to hide part of its balance sheet in partnerships, this policy should be clearly stated in its charter for all to see. Then shareholders will be warned, and the value of the stock will be lower to reflect this.

## Honest Statements

Likewise, the Law of the Market would require that when the executives or board members of a corporation make public statements about its prospects, these are to be honest, unless the charter lets the company spokesmen lie. If the charter does not state that they may lie, they should be legally required to tell the truth to the best of their knowledge.

It is tragic that many Enron employees put much of their retirement funds in the company's stock. One of the basic principles of personal finance is to diversify your portfolio. "Don't put all your eggs in one basket" is age-old advice many of us learn from our parents.

This should be a financial lesson for everybody. Markets are efficient because the ineffective firms fail and go out of business. Most investors don't know what is going on inside a company. It can look good on the outside but be crumbling on the inside. Even those working for Enron did not know what was really going on, yet many put most of their retirement funds in the company's stock. A general rule for investing is not to put more than 5 percent of your assets in the stock of any one company.

The Enron problem was not a fault of the market, but a violation of the ethical rules of the market. There will always be those who try to defraud others. That is why we need laws against theft and fraud. The Enron debacle is the fault of government for not having a clear Law of the Market making auditing conflicts illegal unless the company charter states that it would engage in such practices. The Law of the Market need not even be a governmental law, but given that governments enact laws against theft and fraud, this one would clarify the property rights involved. A company should be presumed honest unless its charter states otherwise, in which case the company's basic documents would be honest.

The pure free market does not include force or fraud, but rather consists of voluntary activity. Vague and confusing government laws and regulations provide the illusion of safety, but actually prevent shareholders and employees from recognizing the risks they are taking. Once again, government, not the market, failed. □

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IDEAS ON LIBERTY
MAY 2002

# A War to End All Banditry

Even before the United States wound down its military operations in Afghanistan, it began looking for targets elsewhere. But policymakers must remember that Washington's primary interest is thwarting transnational terrorists who target Americans, not combating local criminals and insurgents around the globe.

After just three months, the Taliban was overthrown, the al Qaeda network was disrupted, and Osama bin Laden was dead or had escaped. There wasn't much more work to do in Afghanistan, so long as the Bush administration did not take on the thankless task of attempting to build a Western-style democracy in Afghanistan. But with al Qaeda operatives active in an estimated 40 countries, a lot of other potential targets beckon. U.S. Representative Todd Tiahrt points to the Philippines: "After Afghanistan, this is the next priority because there are Americans at risk."

However, intervention in the Philippines risks sucking the United States into conflicts that affect America only tangentially, if that. The archipelagic nation has long faced an insurgency among its minority Muslim population. The conflict waxes and wanes, seemingly insoluble but never threatening the Philippine stability, let alone American security. Commanding most recent attention is the Abu Sayyaf gang, which seized three Americans last year. In November Lt. Commander Jeff Davis, spokesman for the Pentagon's Pacific Command, claimed that Abu Sayyaf was "an international terrorist group that poses as much of a threat to the U.S. as to the Philippines."

The Bush administration subsequently announced $92 million in military aid, rushed in nearly 700 military advisers, and offered combat troops. Manila eagerly accepted the cash and advice. And although it rejected the troops—the Philippine constitution prohibits operations by foreign forces—the Americans will be armed and authorized to defend themselves. Moreover, constitutional objections in a country where the previous president was ousted last year in a soft coup, after the military withdrew its support, might eventually fade.

There is, however, no national security justification for American involvement. Abu Sayyaf's ties to al Qaeda are peripheral at best. Its now-deceased leader fought in Afghanistan against the Soviets; bin Laden's brother-in-law, Mohammad Jamal Khalifa, seems to have channeled some money to Abu Sayyaf.

However, the group operates more like bandits than terrorists. Although they have routinely demanded the release of Ramzi Yousef, mastermind of the 1993 World Trade Center attack, they have been satisfied with bountiful ransoms—collecting about $20 million in 2000, which they used to stoke their arsenal and attract recruits.

Abu Sayyaf has shown no interest in conducting a serious campaign against the United States. Rather, its American victims

*Doug Bandow, a nationally syndicated columnist, is a senior fellow at the Cato Institute and the author and editor of several books.*



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have been targets of opportunity, visiting the wrong resort at the wrong time. It's awful when it happens, but it's not unusual in what remains a dangerous world.

Nor is there any reason the Philippines should be unable to bring the bandits to justice. Manila has more than enough troops, and they are better equipped than the guerrillas. By the end of last year as many as 7,000 soldiers were searching for a band thought to have dwindled to the dozens.

Unfortunately, the Philippines has only itself to blame for its failure. In fact, Abu Sayyaf has taunted the United States about how American weapons shipped to Manila regularly end up in its hands. Bribes to military commanders have apparently helped gang members escape from government attacks.

Training, advice, and equipment from America might help. But the Philippines' economic and political problems run deep. Coup rumors circulated last fall, for instance, and before that the Arroyo administration declared a state of emergency to combat what it claimed was another plot. Until Manila successfully addresses its own failings, it is unlikely to develop the kind of honest and loyal institutions necessary to eliminate groups like Abu Sayyaf.

Out of frustration with Filipino ineffectiveness, Representative Tiahrt, who represents the home district of the captured missionaries, Martin and Gracia Burnham, flew to Manila to urge President Gloria Macapagal Arroyo to accept the intervention of U.S. troops. Victorino Matus of the *Weekly Standard* says simply: "send in U.S. Special Forces."

Yet the reason for such intervention has nothing to do with American security. Writes Matus: "it is—or should be—absolutely imperative for the United States to do whatever it takes to free its own people." Tiahrt sounds the same trumpet: "if it were for me, and I'm sure if it were for you, as an American, you'd hope America would come to your rescue." But U.S. foreign policy should not be driven by the activism of one particularly dedicated congressman. So Tiahrt is calling for development of a consistent American strategy of intervention.

But general human rights cases are problematic. When President Bush presented his ultimatum to the Taliban government last fall, he demanded not only the surrender of bin Laden but also the release of two American Christians charged with proselytizing. Diplomatic and public pressure to gain respect for human rights is assuredly a good thing, but not military action to enforce the same.

Intervention is usually least appropriate when the abuses are committed by unofficial groups. The right strategy is to leave the resolution of most hostage crises to local governments. Official involvement automatically raises the stakes.

## A Way to Draw in Washington

Moreover, military intervention sucks the United States into what are usually broader conflicts ill-suited to easy resolution. Indeed, a consistent policy of rescue provides a trigger by which antagonists can consciously draw in Washington.

Americans, whether busy making money, playing tourist, proselytizing their faith, or doing good works, should not expect to be backed by a Marine Expeditionary Force.

For instance, the Burnhams, missionaries since 1986, are admirable folks. So is Clark Bowers, kidnapped by an Afghan tribal warlord while attempting to deliver medical supplies. But traveling and living abroad carry risks that should be borne by those who choose to accept them.

Of course, standing aloof may seem hardhearted. But I visited Kosovo in 1998 and eastern Burma in 2000, both engulfed in guerrilla war, and Ambon, Indonesia, in 2001, in which a still-dangerous cold war followed two years of Muslim-Christian violence. I took what I considered to be reasonable risks. Had I miscalculated, however, I did not expect the cavalry to arrive. So far, the war on terrorism has been a dramatic success. But there's more to be done. Washington needs to keep its focus on combating transnational groups that threaten the American people at home.

America need not take on responsibility for eradicating banditry the world over. □



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IDEAS ON LIBERTY
MAY 2002

# Credentials: Because the Free Market Abhors a Vacuum

*by Keith Wade*

Many people gripe about credentialing. The requiring of a credential, it is said, shuts qualified people out of the labor market (much as my lack of demonstrated athletic prowess keeps me from getting that job as an NFL quarterback that I very much want!).

Before discussing why credentials have become such an important part of today's employment market, let me admit my biases: I am the director of certification for the Polk County, Florida, chapter of the Institute of Management Accountants and the string of letters behind my name stands for Certified Management Accountant, Certified in Financial Management, and Certified Novell Administrator.

Back in the "good old days" (and as a relative youngster the good old days I'm speaking of weren't so long ago), there were some assumptions one could make. Second-graders could read, because on the first day of first grade one began reading aloud by sounding out the letters and one certainly did not get promoted to second grade without demonstrated reading skills. One got all the self-esteem one needed after *successfully* sounding out "Midnight, the cat" in one's reader. A high-school diploma meant that one could read, write an expository essay, do addition and multiplication, and show up for class on time. While IQ testing had been passé for decades, its closely correlated cousin—the SAT score—remained a much-quoted and asked-about number with powerful predictive abilities. A bachelor's degree meant that one was skilled in the "liberal arts" and had been vested with—perhaps forgotten, but at least exposed to—the common body of knowledge possessed by "educated people." And so forth. . . .

The good old days were replaced by the era of self-esteem (warranted or not). While caring teachers had always promoted self-esteem, now it was tied to *effort* rather than *results*. (Rather than feeling good about *learning* the multiplication tables, for example, it's okay to feel good about *trying* to learn them irrespective of success.) Trying hard went from being a tool for doing well to being a substitute for doing well. "Social promotion"—the practice of promoting students to the next grade regardless of whether they had mastered the current grade level—meant that one could no longer assume that second-graders could read. A "high school equivalency" certificate became the de facto equivalent of a high school education. Allegations—and acceptance of these allegations at least among a preponderance of laypeople—of cultural bias in the SAT led to its diminished importance. Grade inflation—and a relaxation of standards at many institutions—meant that even a college degree

*Keith Wade, CMA, CFM, CNA (keithwade@usa.net) is the vice president of administration and chief financial officer at Florida Cypress Gardens, an adjunct professor of business at Webster University, Lakeland, and a doctor of business administration student at Argosy University, Sarasota.*



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was not in all instances a guarantee that its possessor was an educated person.

The free market, as we have seen time and time again, abhors a vacuum. Employers have to make decisions; they cannot hire everyone and see who works out best (nor can they afford repeatedly to hire the wrong candidate). They need to screen potential employees to select those who have the best chance at success. When their tools to do this degraded, they created their own. Among these was the requiring of credentials.

Credentials are, at their very core, the essence of the free market. The issuer of the credential sets—and publishes—the criteria for obtaining it. It is obviously in the best interest of the credentialing body to insure that its credential is widely respected as a predictor of success. Those obtaining a given credential, and those requiring it, can decide for themselves what value the credential has. The entire transaction is voluntary.

## Fair to the Core

Credentials are also, at their very core, fair. Irrespective of one's culture and demographics, either one has what it takes to earn a credential or one does not. Even fairer, one has the choice of whether to earn a credential or not. Fairer still, employers have the right to decide whether or not any specific credential has any value. They level the playing field by allowing one to demonstrate that—everything else aside—one possesses the knowledge (or other defined skills or background) required to obtain that certification.

Credentials have become popular—almost a de facto requirement for some positions—because they perform a valuable service: they objectively demonstrate that their holder possesses some quantifiable, objective skill, knowledge set, or other element. For example, I do not know—and it would be tough to discern in an interview and impossible to discern from a résumé—whether you took cost accounting, whether you had a good teacher, or whether the teacher covered the material. If, however, you show me your Certified Management Accountant certificate, I know that you—like everyone else with that certificate—have significant knowledge of cost accounting. Credentials are even more powerful when nontechnical managers need to hire technical staff. I am not technically qualified, for example, to quiz someone on his router knowledge. If, however, he has a Cisco certification, I know he has the technical skills required (without even knowing what these technical skills are, much less how to test for them).

Like most free-market solutions, credentialing is a win-win proposition. The potential employer wins because he can quickly discern a great deal about a candidate by his possession of a relevant credential. Conversely, the employee wins because he can definitively demonstrate a great deal about his skills and knowledge by earning the appropriate credential. Society wins too. Not just because the entire process is voluntary, but also because the efficiencies involved in hiring the right person as expediently as possible are built—albeit indirectly—into the prices of the goods we consume and the services we use. □



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IDEAS ON LIBERTY
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# Medical Technology and the State

*by Gary M. Pecquet*

So-called public-policy experts often take the many advances in modern technology for granted. They assume that government regulations and controls merely redistribute the fruits of progress without affecting the nature and extent of technological development itself.

But that is wrong. Whenever the government involves itself in the financing and distribution of goods and services, the production of those things will also be affected. Only certain social institutions have proven capable of delivering sustained economic growth. Private ownership of the means of production and free markets provide the necessary environment for entrepreneurial risk-taking and innovation. It is never enough for some government laboratory to develop a new technology. New technologies must prove to be cost-effective in a market context in order to successfully serve the needs of customers over time.

In free markets technological advances tend both to improve the quality and to reduce the costs of goods and services sold to consumers. The histories of the automobile and pocket calculator are typical. First, producers introduce a new product as an expensive luxury item, affordable only to the rich and sought chiefly as a curiosity. Second, competition among businessmen for profits leads them to seek larger markets for the products. Consequently, the producers direct considerable attention to developing cost-reducing innovations (for example, introduction of assembly-line production techniques by Henry Ford and the use of microchips in calculators). Third, entrepreneurs vigorously compete and pass on these cost reductions to consumers through lower prices. Fortunes are made and lost, but the new technologies raise the living standards for everyone.

Advances in medical technology, however, have failed to reduce the cost of health care. The introduction of more and more new medical techniques and equipment only seems to push costs ever upward. Overall health expenditures increased from 5.9 percent to about 14 percent of gross domestic product from 1965 to 2001 and are expected to grow to 16.2 percent of GDP by 2008.[1] Some experts have even blamed the new technologies for the cost explosion. Henry Aaron, senior fellow at the Brookings Institution, recently asserted that medical spending continues to rise faster than the GDP because the population is growing and new medical technologies and therapies are constantly being developed to enable more people to receive treatment than previously possible.[2]

Professor Mark Pauly of the Wharton School of Business stated, "Basically, most of the data I know about indicates that the lion's share—whatever that is—of the growth in medical spending per capita, even

*Gary Pecquet (gpecquet@aol.com) is an economist and C.P.A. in the greater New Orleans area.*



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after you adjust for the aging population, is accounted for by what we call technology."[3] For example, before the development of hip-replacement surgery, an arthritic hip was treated with aspirin and a walker. Now a single hip replacement can cost from $20,000 up to $50,000 depending on age and the length of hospital stay.[4] Advances in medical equipment also seem to drive medical expenses ever upward. MRI (magnetic resonance imagery) machines involve both heavy capital outlays and additional personnel. The average x-ray costs $80 while a similar MRI machine costs over $1,200 per examination. Unlike x-rays, MRIs can detect brain and muscular disorders.[5]

## Different Method of Payment

The method of payment sets health care apart from most consumer goods. Most goods are purchased directly by the consumers who enjoy them. In contrast, about 85 percent of all health-care expenditures are financed through third parties. The federal and state governments under Medicare and Medicaid pay 44 percent; private insurance companies and other third-party payers pick up 39 percent.[6] Medicare subsidizes the health care of those over 65 years old and Medicaid provides free benefits to the poor. Both programs were enacted in 1965. Private insurance is also encouraged under federal law, which exempts employee medical benefits from income taxes. Since the government now spends huge sums on health care, it decides which technologies and procedures will be covered under its programs. Once a procedure makes the list of acceptable (nonexperimental) practices under Medicare, the standard is set for most private insurance plans to follow. The quality of medical cares improves, but the costs increase.

Under government-financed third-party payments, every new technological novelty becomes available to the vast majority of the American public—before the cost-reduction stage can occur. Medical technology entrepreneurs need not reduce costs to broaden their markets! Consequently, entrepreneurs of medical technology focus on newer, even more expensive technological improvements, rather than on applying costs-reduction methods to existing technologies. For example, some new antibiotics may be only 2 percent more efficacious and yet cost 100 percent more. But drugs do not have to be marketed to a cost-conscious public. As long as the new drugs obtain approval under Medicare rules, doctors and patients will avail themselves of the best possible quality—at taxpayer expense.

Normally, technological advances are a benefit to producers and consumers alike. Government financing, however, introduces a third party—the taxpayer—who is bled dry. State governments have attempted to restrict health-care technology by requiring providers to obtain licenses called "Certificates of Need" (CON) from state officials in order to purchase new equipment. CONs supposedly reduce government expenditures by making medical technology less available, just as socialized medicine does in Canada. This approach to cutting medical costs frequently leads to political scandals and long waits. Most important, it does nothing to redirect entrepreneurs toward reducing costs.

Countries with nationalized health care, such as Canada, Germany, and the United Kingdom, spend much less on medical care than the United States (only 7–10 percent of GDP compared to 14 percent in the United States).[7] This is not because the government is more cost-effective than health-care markets, but because there is little innovation under a nationalized system. By restricting technological advances and cutting the quality of medical care to the bone, socialized medicine can offer lunchbox medical care to everyone, but even then routine office visits and surgeries often require waiting in long lines. During the '80s middle-class Canadians began to flock to the United States for treatments.[8] Since then, the long lines for Canadian specialists have dramatically increased. The required median waiting time for Canadian patients between referral by a general physician and actual treatment by a specialist increased from 9.3 to 16.2 weeks



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from 1993 to 2001; and for certain specialists, such as orthopedists and neurosurgeons, the wait has stretched to about six months.[9]

Under these circumstances, med-tech entrepreneurs need not serve individual patients and doctors. Cost reductions will not be forthcoming under government-financed egalitarian health care. It is no accident that the United States, where health-care financing is only partially socialized, health-care attracts more new investments in medical technology than Canada or Europe, where government-funded health care is complete. In 1990 the state of Washington had more MRI machines than all of Canada, even though Canada's population of 26 million is more than five-and-a-half times larger than Washington's population.[10]

It is also no accident that the proponents of nationalized health care in the United States frequently blame the very creators of new medical technologies (especially the pharmaceutical companies) for the cost overruns inherent under government funding. The all-too-eager national health-care chefs impatiently wait for the proverbial golden goose to be added to their stewpot.

## Moral Vision

Beneath every public policy lies both an economic theory and a moral vision. The economic theory on which Medicare and Medicaid are based asserts that third-party payments will not significantly alter the behavior of patients, doctors, and other health-care providers—including med-tech entrepreneurs. In 1965 when Medicare and Medicaid were enacted the federal government paid most medical expenses without questioning the decisions made by doctors and patients. But one cannot be personally responsible without being fiscally responsible: people flocked to receive taxpayer-paid medical care and they tended to opt for the most expensive treatments available.

Medicaid costs quickly got out of hand. Outlays increased by an average 36.6 percent per year from 1967 to 1972, and about two-thirds of this increase came from the sheer numbers of eligible welfare recipients.[11]

Medicare expenses grew slowly at first because eligibility depends on reaching 65. From 1970 to 1981, the number of Medicare enrollees increased by only 3.1 percent,[12] but the cost increases began to soar out of control by the mid-1970s. During the period 1974–1981 the cost increased annually by 19.7 percent, 30.3 percent, 20.3 percent, 21.2 percent, 17.0 percent, 15.6 percent, 20.2 percent and 21.3 percent.[13] A significant portion of these Medicare cost increases came from improvements in the quality of health care due to the introduction of new medical techniques and technologies. Periodically, Medicare has been projected to go bankrupt and politicians have responded by raising taxes and restricting services. By the year 2000, spending on Medicare physician services was growing 5 percent faster than GDP, and the Medicare Board of Trustees expected the program to exhaust its funds by 2023.[14]

Government-financed health care is not a miracle cure for those who cannot afford treatment: the inevitable consequence of divorcing the consumption of health services from cost considerations leads to bankruptcy and/or Draconian government restrictions and rationing. Under socialized medicine in Britain, Canada, and elsewhere patients die as they wait for treatment. Others cope by receiving antiquated treatment. Expensive kidney dialyses or the latest cancer therapies may be routinely denied to old people. Inevitably, the government must control costs somehow, so it begins to deny modern treatment to the sick and allowing the severely ill and old to die.[15]

The moral vision that underlies Medicare, Medicaid, and the push toward "universal coverage" over the recent decade is found in the discredited Marxist credo that goods should be "distributed" according to need, rather than exchanged according to "ability to pay." Government intervention in health care is a poisoned pill marketed under many different brand names: "single payer," "mandatory co-ops" with "universal coverage," private insurance under "community rated" pools financed under "employer mandates" (the Clinton plan), Medicare, and



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*The "feel good" credo "from each according to his ability to each according to his need" does not only lead to economic bankruptcy; it generates moral bankruptcy as well. By removing doctors and patients from the cost-awareness loop, people are deprived of personal responsibility.*

Medicaid. Each of these pills contains the same deadly ingredient with only slight differences in the sugar coating. Each relieves patients and doctors of cost consciousness—by design. Each turns technology from everyone's friend to a dangerous budget buster, which the government must throttle and ration.

The "feel good" credo "from each according to his ability to each according to his need" does not only lead to economic bankruptcy; it generates moral bankruptcy as well. By removing doctors and patients from the cost-awareness loop, people are deprived of personal responsibility. Individuals no longer must choose between alternative methods of treatment based on cost differences. Nor must they face tough decisions such as choosing between selling the house and sacrificing Junior's college education in order to prolong Granny's life a few more weeks by using the latest life-support equipment.

Approximately 1 percent of GDP is spent on the dying in their last year of life,[16] and about 40 percent of these costs are incurred treating patients during their final 30 days of life.[17] However, averages can be deceiving. Only about 3 percent of Medicare patients who die actually incur the exorbitant costs due to aggressive care.[18] A comparatively small number of patients are responsible for a lion's share of the costs of dying.

Terminal medical costs paid by conscious recipients or their loved ones may be well worth the price. But dying patients are sometimes unable to make choices for themselves and are forced to undergo invasive high-tech procedures that merely extend the dying process for a short time. Third-party insurers, including Medicare and Medicaid, expend enormous taxpayer funds to relieve patients and their loved ones from making informed cost-conscious decisions. Already one state, Oregon, has followed the lead of the socialized medical-care nations and adopted health care rationing by denying certain treatments to the old or very sick.[19] Do we want to follow this lead?

Choices between one's wealth and the health of a loved one are often difficult, but a morally responsible life often involves difficult choices. Are we really better people for abdicating them to politicians and bureaucrats? One of the most appealing aspects of socialism to some people is that the government relieves them of the need to make difficult choices. The Soviet system once promised the people that the basic necessities would be provided to all who obeyed. Under government health care the state either provides the most expensive options or else it rations care in a manner that removes all the cost considerations from the relevant parties.

National health insurance damages people because it treats them like children. Government planners decide how much medical technology we should have and who shall receive its benefits. Individuals are discouraged or deprived of the ability to save for their medical emergencies and old-age care. Individuals are denied the opportunity to reduce health-insurance premiums by lifestyle changes. Individuals are even prevented from allocating their own health-care dollars by shopping for an insurance package tailored to their personal needs.

Government-financed medical care may make some people feel better, but is this "feel good" credo a moral principle worth



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upholding? Esau sold his precious inheritance to Jacob for a bowl of soup. Is a bowl of public health worth giving away the prospects of continued medical improvements for generations to come?

The recent proposals stemming from the 2000 election to expand Medicare to cover prescription drugs only continue the trend toward nationalized health care. We must reverse that trend and begin adopting approaches that restore cost-consciousness to patients and doctors, such as medical savings accounts. Insurance companies should be free to set premiums according to medical risk instead of according to a "community rating," which ignores differences among the insured.

Only when we become responsible for our own health care will med-tech entrepreneurs compete to reduce medical costs. These cost reductions are needed to make room for wave after wave of still newer medical technologies that will enable us to live longer, healthier lives. □

1. Steve Eisenberg, medical director of Blue Cross Blue Shield of Minnesota, September 19, 2001, at www.ssc.k12.mn.us/insuradvminutes.htm.

2. Geri Aston, AMNews staff, "Medicare sound for now, but long-term outlook is gloomy," April 17, 2000, *Amednews.com: The Newspaper for America's Physicians*, at www.ama-assn.org/sci-pubs/amnews/pick_00/gvl10417.htm.

3. "Health Policy Discussion" from "Productivity in Health Care: The Value of Medical Technology," AEI Conference, February 28, 2001, at www.newt.org/forum_aei_health.htm.

4. Leigh Hopper, "Hip replacement firm issues recall," *Houston Chronicle*, January 23, 2001, at www.chron.com/cs/CDA/story.hts/topstory2/788942.

5. Mark H. Gurda, "Rising costs, September 18, 2000," at www.healthinsure.com/rising_costs.html.

6. Calculated from a report by the Health Care Financing Administration, "Table 3 National Health Expenditures Aggregate and Per Capita Amounts, Percent Distribution and Average Annual Percent Change by Source of Funds: Selected Years 1982–2010." (Calculations based on the 2000 projection.) See www.hcfa.gov/stats/NHE-proj/proj2000/tables/t3.htm.

7. In 1997 the percentage of GDP spent by these nations on health care was: United States, 13.6 percent; Canada, 9.3 percent; Germany, 10.4 percent; and the United Kingdom, 6.7 percent. (International Health Policy, "Multinational Comparisons of Health Care," www.cmwf.org/programs/international/ihp_1998_multicompsurvey_299.asp#expenditures.)

8. Jarret B. Wollstein "National Health Insurance: A Medical Disaster," *The Freeman: Ideas on Liberty,* October 1992. The article is available online at www.fee.org.

9. Michael Walker and Greg Wilson "Waiting your Turn: Hospital Waiting Lists in Canada," 11th edition, Fraser Institute, graph at www.fraserinstitute.ca/publications/critical_issues/2001/wyt/section_05-1.html.

10. John C. Goodman and Gerald L. Musgrave, "Twenty Myths about National Health Insurance," National Center for Policy Analysis, 1991, cited in Wollstein.

11. John Holahan, *Financing Health Care to the Poor* (Lexington, Mass.: Lexington Books, 1975), pp. 28–29; cited in Paul B. Ginsburg, "Public Insurance Programs: Medicare and Medicaid," in H.E. Frech, ed., *Health Care in America: The Political Economy of Hospitals and Health Insurance* (San Francisco: Pacific Research Institute for Public Policy, 1988), p. 190.

12. Ginsburg, p. 188.

13. Ibid., Table 5–1.

14. Geri Aston, "Medicare sound for now, but long-term outlook is gloomy," April 17, 2000, *Amednews.com: The Newspaper for America's Physicians*, www.ama-assn.org/sci-pubs/amnews/pick_00/gvl10417.htm.

15. Goodman and Musgrave, pp. 29–31, cited in Wollstein.

16. Author's computation. About 30 percent of all Medicare money is spent on those who die in the same year the money is spent. J.D. Lubitz and R. Prioda, "The Use and Costs of Medical Services in the Last Two Years of Life," *Health Care Financing Review* 5 (1984), pp. 117–31.

17. J.D. Lubitz and G.F. Riley, "Trends in Medicare Payments in the Last Year of Life," *New England Journal of Medicine* 328 (1993), pp. 1092–96.

18. See Lubitz and Prioda, and Lubitz and Riley.

19. "The Grand Unification Theory of Health Care," Section 7, "Rationing and Death–Covert Rationing and End-of-Life Care," www.yourdctorinthefamily.com/grandtheory/section7_1.htm.



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IDEAS ON LIBERTY
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# The Courageous Decision That Lasted But Nine Days

*by Joseph S. Fulda*

Sonya Evette Singleton is not a heroine, but for nine days her case shaped the law in the tenth judicial circuit of the United States and opened the doors for a bit more honor in government.

Ms. Singleton had been convicted of conspiracy to distribute cocaine and of money laundering, based partly on the testimony of one Napoleon Douglas, an accomplice to her offenses.

A three-judge panel of the Tenth Circuit, including its Chief Judge, asked why Mr. Douglas would possibly sell out a confederate. It turned out there were three reasons: First, the prosecutor had promised not to bring any additional drug charges against him; second, the prosecutor had promised to recommend a lightening of his sentencing for the charges already filed, or so Mr. Douglas believed; third, the prosecutor promised to inform the Mississippi parole board of Mr. Douglas's material assistance in obtaining the conviction of Ms. Singleton and others. The prosecutor made these promises to Mr. Douglas in consideration of his testimony, a rather unsurprising practice in the case of victimless crimes since without some kind of sting operation the absence of a victim who is harmed makes it impossible to prosecute these crimes.[1]

*Contributing Editor Joseph Fulda (fulda@acm.org) is the author of* Eight Steps towards Libertarianism *(Free Enterprise Press).* *Copyright Joseph S. Fulda 2002.*

There is only one problem with this mode of operation: *It is illegal.* § 201(c)(2) of Title 18 of the United States Code *forbids* giving "anything of value" in consideration of testimony. The panel of judges considered whether this applies to the government too. There were also questions raised by three precedents in other circuits. Among the issues were a ruling that something relatively "intangible" like a liquor license was not a thing of value and that a promise made to secure the status quo was not consideration. The panel made short shrift of these arguments:

> We agree with those circuits which have held that the test of value is whether the recipient subjectively attaches value to the thing received. . . . In this light we apply the statutory phrase "anything of value" to the promises made to Mr. Douglas. The obvious purpose of the government's promised actions was to reduce his jail time, and it is difficult to imagine anything more valuable than personal physical freedom. . . . In the case of the promise not to prosecute, the value was even greater: besides guaranteed physical freedom he was guaranteed freedom from the burden of defending himself and from the stigma of prosecution and conviction as well.
>
> Our basis for determining these promises were of value is that the record indicates Mr. Douglas subjectively valued



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them. They were all he bargained for in return for his testimony and guilty plea.

And:

> We are likewise unpersuaded that preservation of the status quo cannot constitute a thing of value. The persuasion of the United States was brought to bear in return for testimony at a time when the witness's status quo (which happened to be ill-gotten gain) was about to change drastically for the worse.

Good Austrian economists!

## Does It Apply to the State?

As to the question of whether the statute applies to the government, the panel's judges later reasoned: "To suggest that government attorneys performing prosecutorial functions are beyond scrutiny because of who they represent is anomalous because it merges attorney and client. . . . Merely because the government cannot be prosecuted if its agents violate a rule does not mean that the rule may be disregarded; to the contrary, the rule may be enforced by means other than prosecution, here by exclusion of evidence."[2]

We think that in the hierarchy of "life, liberty, and property," liberty clearly comes before property—and if Patrick Henry is the model, before life, as well. Yet, surely, no one would regard a witness whose testimony was obtained by bribery—*property* in exchange for "evidence"—as credible, and no judge aware of the bribe would allow the "witness" to testify in his courtroom. Yet uncounted thousands of prosecution witnesses are bribed by an offer of *liberty*—no charges, reduced charges, or less time under lock and key. Such witnesses are said to "turn state's evidence," and, indeed, the evidence is turned—from credible to inescapably tainted. There are few men who would not commit perjury to escape prison time, and to allow testimony against a defendant to be received in evidence when the alternative is the terrifying prospect of incarceration is simply unconscionable. It is, simply put, state bribery and subornation of perjury. No principle is more self-evident than that nothing can be believed of a witness with a gun to his head. Thus we no longer exact "confessions" from defendants by force or threat of force. To do so from his alleged accomplices is not much more credible—or honorable.

The panel also spoke to this issue, although in terms more muted than we just have:

> If justice is perverted when a criminal defendant seeks to buy testimony from a witness, it is no less perverted when the government does so. Because § 201(c)(2) addresses what Congress perceived to be a wrong, and operates to prevent fraud on the federal courts in the form of inherently unreliable testimony, its proscription must apply to the government.

Alas, the decision, correct legally and morally, was not to stand. Nine days later, the entire U.S. Court of Appeals for the Tenth Circuit *acting on its own motion* voted to vacate the panel's decision and to rehear the case *en banc*. Although all three judges on the original panel dissented, every other circuit judge voted with the majority to allow this offensive evidence-buying practice. They did this so quickly that the *Federal Reporter*, a compendium of appellate court decisions published quasi-privately by the West Publishing Company, contains no record of the panel's original decision. The vacated decision is also gone from the Lexis and Westlaw legal databases, which are also only quasi-private; this, even though the first word on top of the original panel decision is "PUBLISH." To find this decision, one has to go to completely private legal resources such as findlaw.com on the Internet.[3] There truth lies buried from sight. □

1. See my "The Pernicious Nature of Victimless-Crime Laws," *Ideas on Liberty*, April 2002, pp. 19–20.
2. *United States v. Singleton*, 165 F.3d 1297, 1311 (10th Cir. 1999) (en banc) (Kelly, J., dissenting).
3. See http://caselaw.lp.findlaw.com/scripts/getcase.pl?court=10th&navby=case&no=973178&exact=1.



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FEE TODAY

www.FEE.org May 2002

# The Map that Predicted the Terrorist Attacks

By Mark Skousen
President, FEE

Take a close look at the chart in the next column and the world map on the next page. They reveal a story that will forever change the way you view the world, especially after September 11, 2001, and how YOU can help fight the war against terrorism.

The chart shows an amazing connection between economic freedom and income. As you can see, the more freedom a nation enjoys, the higher its standard of living, as measured by per capita income in purchasing power terms. The chart conveys two simple messages.

## Message #1: Economic Freedom Leads to Prosperity

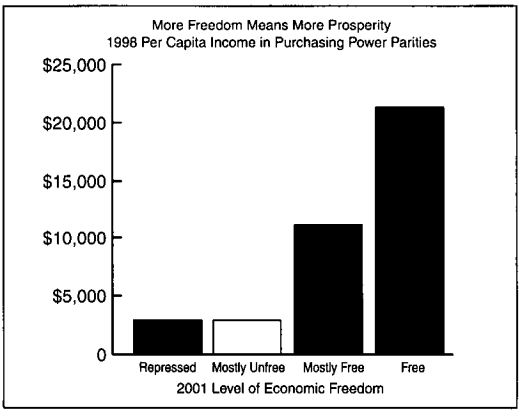
Despite the good intentions of those who support government intervention, regulated economies, and redistribution of wealth, the free market is the surest way to provide the highest standards of living for all people.

## Message #2: Free Markets Lead to Peace

Free markets mean more than higher income. They also lead to international security. Look at the "world map of economic freedom" on page 2. This map, published prior to the terrorist attacks on September 11, 2001,[1] reveals with unmistakable clarity why Islamic extremists killed over 2,500 people in New York and Washington, and more importantly, it shows how we can prevent terrorism in the future.

Each nation is scored and ranked according to its degree of economic freedom, based on ten factors, such as level of taxation, trade restrictions, labor regulations, inflation, property rights, and government intervention in the economy. Each country is denoted by color, from blue to red, similar to the bar chart.

**Economic Freedom and Per Capita Income**




Source: The World Bank, 2000 World Development Indicators.

[1]This map appears in a book titled *2001 Index of Economic Freedom*, published jointly by the Heritage Foundation and the *Wall Street Journal*. The book is updated yearly.



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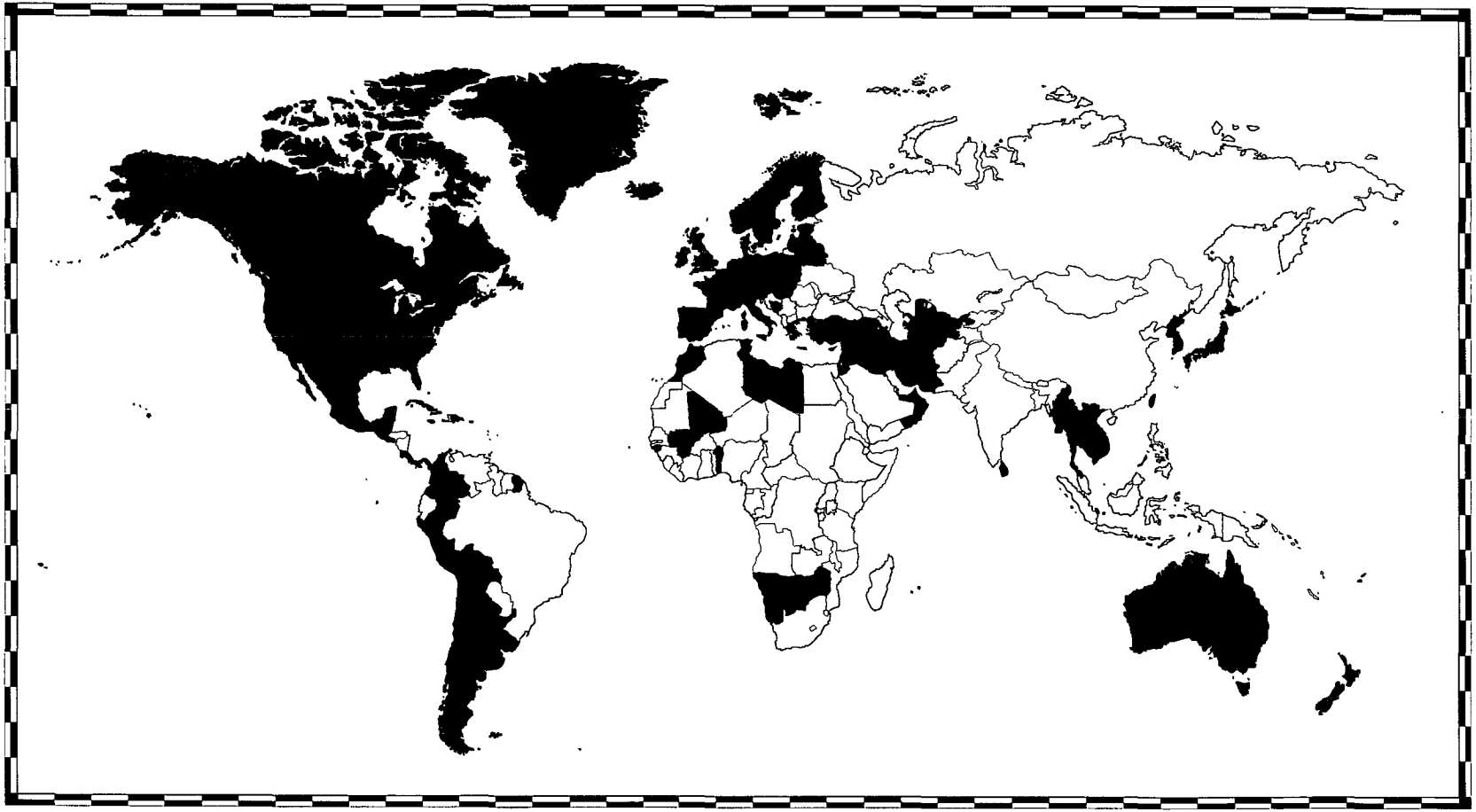
# World Map of Economic Freedom



Free
Score: 1.00 to 1.95

Mostly Free
Score: 2.00 to 2.95

Mostly Unfree
Score: 3.00 to 3.95

Repressed
Score: 4.00 to 5.00

Not
Ranked

Courtesy: The Heritage Foundation

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Countries colored blue are ranked "free." Countries colored green are considered "mostly free." Nations colored yellow are labeled "mostly unfree." And nations colored red are ranked "repressed."

This unique world map is an eye-opener. Note the following:

- **First, only a few countries are "free."** Only a dozen countries around the world are colored blue, including the United States, Ireland, Britain, Switzerland, Australia, New Zealand, and Hong Kong. True freedom is a rare and delicate flower.
- **Second, Canada, Latin America, and Europe are "mostly free."** Some Americans may be surprised to see Canada listed as "mostly free." But Canadians are not surprised—they know that Canada has a much bigger welfare state than the United States. The same holds true for Europe. Despite efforts to create a "United States" of Europe (the European Union), Europe remains a highly regulated welfare state.
- **Third, nations in the Third World are "mostly unfree."** Countries painted yellow include Russia, China, India, Brazil, and most of Africa. In fact, of the 155 nations surveyed, over half (81) received a negative grade ("yellow" or "red").

## Look Where the Red Is!

**The biggest shock is this: nearly all the red is located in the Middle East.** The connection is clear: terrorism and poverty go hand in hand with repressed freedom. Despite an abundance of oil reserves, most Arabs live in shockingly deep poverty, governed by leaders who oppress their people economically. The region has been crippled by constant war, corruption, inflation, black markets, protectionism, and government intervention on a grand scale. Most of the Middle East continues to suffer from economic depression, political turmoil, and military conflict. And, as we have seen, countries there are also steeped in terrorism.

Henry Hazlitt, a FEE founding trustee and author of *Economics in One Lesson,* summed it up well: "It is socialist governments, notwithstanding their denunciations of imperialist capitalism, that have been the greatest source of modern wars."

## The Most Important Lesson in the War on Terrorism

What is the most important lesson we can learn from this map? Simply this: **Economic repression breeds fanaticism and terrorism.** It is not surprising that the Middle East is a major source of radicalism today. A closed society breeds intolerance and fanaticism. Interestingly, most of the Middle East is also famous for its lack of political democracy and religious tolerance. Most are ruled by dictators or kings. Religious proselyting is prohibited in Arab nations and even in Israel.

## How to Permanently Win the War Against Terrorism

But there is another important lesson to learn from this map. **Liberalized trade and open markets break down cultural and social monotheism and destroy fanaticism and intolerance.** Adam Smith, the Scottish economist and founder of market capitalism, and Charles Montesquieu, the great French philosopher, taught this vital doctrine. "Commerce cures destructive prejudices," Montesquieu wrote in *The Spirit of the Laws.* "It polishes and softens barbarous mores. . . . The natural effect of commerce is to lead to peace." Adam Smith added that the commercial society moderates the passions and prevents a descent into a Hobbesian jungle of greed and hate.

Business encourages people to become educated, industrious, and self-disci-



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plined. Commerce encourages trade, travel, and exchange among nations and cultures. Business people are the ultimate in practicality—by nature open-minded and tolerant of other viewpoints. Their goal is to provide what others need, at a price they can afford. As John Maynard Keynes once said, "It is better that a man should tyrannize over his bank balance than his fellow-citizen."

**What then is the real solution to the war on terrorism?** Sending troops and fighting war in faraway lands may offer a short-term solution to terrorism, but real, permanent peace can only be achieved through opening trade and business, and establishing a legal system conducive to a civil society and prosperous economy. A good dose of open markets and competition in all walks of life could go a long way toward bringing peace, prosperity, and good will to this dangerous part of the world. Until that happens, however, many will shout "peace, peace, when there is no peace." (Jeremiah 8:11)

## Help Color the World Blue!

The bar chart and the world freedom map also give us the opportunity to explain our mission here at FEE. Simply put, our goal is to color the world blue, to maximize freedom for all people in all lands. It's a tall order, but we are determined to create more "blue" countries wherever possible.

How do we at FEE fight terrorism? By expounding sound free-market principles both here and abroad to students, teachers, business people, and the general public—to anyone who will listen.

I have traveled around the globe to 64 countries—in North America, Europe, Africa, Asia, Latin America, and the Middle East—and talked to people of all walks of life about the liberating effects of the free-enterprise system. They have asked for our help in bringing *Ideas on Liberty*, books, pamphlets, and seminars to them and teaching others about the benefits of a free society.

I do think that we are making progress. If this world map of economic freedom had existed in 1985, when the Soviet Union and China were closed communist nations, over half the world's population would have been colored "red." But with the collapse of the Berlin Wall and the downfall of Soviet communism, many nations have moved from "red" to "yellow" and from "yellow" to "green." Will they eventually move to "blue"? Through our ever-expanding programs, FEE will do everything in its power to achieve this lofty goal.

How can you help? Pass along this special issue of *FEE Today* to your friends, relatives, and business associates. Show them how freedom and prosperity are closely linked. If we lose our freedom, you can be sure that our standard of living will decline. But more importantly, show them how free markets lead to the end of terrorism, intolerance, and oppression.

Please consider making a donation to FEE, which will help spread ideas on liberty and sound economic thinking throughout the world. If you give any amount over $39, you will receive a year's subscription to *Ideas on Liberty.*

Keep the light of freedom alive.

Mark Skousen

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IDEAS ON LIBERTY
MAY 2002

# The Maternity Hospital and the Mental Hospital

At first sight, the maternity hospital and the mental hospital are two completely different institutions. However, on closer examination, striking similarities emerge.

Neither pregnancy nor delivery is a disease; each is an aspect of the mammalian reproductive mechanism. Women delivered babies long before there were special buildings called "lying-in hospitals" established to care for them. Behavioral reactions to the vicissitudes of life are also not diseases; they are aspects of the repertoire of human actions. In the past, people who displayed such behaviors prospered or perished, were celebrated or condemned, long before there were special buildings called "mental hospitals," ostensibly devoted to their care.

Modern medicine begins in the middle of the nineteenth century, with the development of the concept of disease as a pathological alteration of cells, tissues, and organs. This new understanding was made possible in part by advances in technology, and in part by the establishment of large municipal teaching hospitals. The live patients were the "case material" for clinical instruction, and when they died their corpses formed the "material" for the pathologist's postmortem examination.

*Thomas Szasz (tszasz@aol.com) is professor of psychiatry emeritus at SUNY Upstate Medical University in Syracuse. This is adapted from what will be an appendix in his forthcoming book,* Liberation by Oppression: A Comparative Study of Slavery and Psychiatry *(Transaction, Spring 2002).*

In England, hospitals began to be established more than a hundred years before the dawn of scientific medicine. These institutions resembled our current nursing homes and hospices more than they resemble our hospitals: they were way-stations to the cemetery. Most of their would-be beneficiaries viewed entering them with the same dread with which people now view entering a nursing home. When persons of rank and wealth fell ill, they were cared for and died at home. The aim of the early hospitals was social reform, not medical healing. Before the twentieth century, women from families with even modest means were rarely, if ever, delivered in maternity hospitals.

The development of mental hospitals followed a similar pattern. The early private madhouses were intended to help wealthy persons dispose of their unwanted relatives, by disguising coerced rehousing as care for insanity. After insane asylums became public institutions, in the eighteenth century, their inmate population consisted almost entirely of paupers. In hindsight, no medical historian doubts that, for the patients, the early hospitals did more harm than good. In the case of mental hospitals, this is still the case, with the judicial system and lawyers as additional beneficiaries.

Prior to the twentieth century, hospitals were places of horror. However, the harm they could do was limited by the fact that most of the sick people who went there were hopelessly ill and would have soon died in any case. This, however, was not true for



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maternity hospitals and mental hospitals. The typical woman who entered a lying-in hospital was young and healthy. She would probably not have died had she delivered her infant at home. Her death was directly attributable to where she delivered, that is, the maternity hospital. Similarly, the typical person admitted to a mental hospital was a young adult in good health. Becoming a chronic mental patient was a direct consequence of being incarcerated for years in an insane asylum.

## Identifying the Real Beneficiary

Looking back at the history of lying-in hospitals, Irvine Loudon, an English medical historian, writes:

> [T]he lying-in hospitals were from the early years plagued by recurrent epidemics of puerperal fever with appalling mortality rates. By *choosing delivery* in a lying-in hospital, women (although they seldom knew it) were exposing themselves to a risk of dying that was many times higher than it would have been if they had stayed at home in the worst of slums and been attended in their birth by no one except family and an untrained midwife. The lying-in hospitals were such a disaster that, *in retrospect*, it would have been better if they had never been established before the introduction of antisepsis in the 1880s. [*The Tragedy of Childbed Fever*, Oxford University Press, 2000, p. 59.]

Two points need to be made about this account. One is that women did not, as a rule, *choose* to be delivered in lying-in hospitals. Typically, they were dragged there by impoverished, overburdened relatives who wanted to be relieved of the duty of caring for them. The other point is that the detrimental nature of the lying-in hospital need not have been a retrospective judgment. It was obvious from the start, to many physicians as well as to many pregnant women. Physicians could not have helped but notice that puerperal fever occurred far more often among women delivered in such institutions than among women delivered in their homes.

During the first half of the nineteenth century, the medical profession, resting on new discoveries in chemistry and physics, began to acquire prestige and power it had not enjoyed in previous ages. Physicians claimed to have an explanation for virtually everything that ailed the human body. Puerperal fever was no exception: it was due to bad air, the so-called miasma theory. A few physicians dissented. In the United States, Oliver Wendell Holmes, and in Austria-Hungary, Ignaz Semmelweis, declared publicly that puerperal fever was a contagious disease, transmitted by the "dirty hands" of the doctors.

This was bad enough. But Semmelweis made another mistake: he proved it. He made medical students and doctors wash their hands with chlorinated lime water before examining patients: "So effective were his methods that between March and August of 1848 no woman died in childbirth in that division," Loudon writes. As a result, Semmelweis became living proof of the Hungarian proverb, "Tell the truth, and people will bash in your head."

Henrik Ibsen's famous play *An Enemy of the People* (1882) is the dramatic story of a doctor whose work and fate are loosely modeled after the tragedy of Semmelweis. Dr. Stockmann, a simple country doctor, tries to protect people from using the town bath contaminated with pathogenic bacteria. His discovery, however, conflicts with people's belief in the therapeutic properties of their treasured spa and jeopardizes their economic interests. The city's leaders and the public denounce Stockman as "an enemy of the people."

The waters Stockman denounced *had* to be therapeutic—lest the city's image be transformed from spa to a source of pestilence. Similarly, antipsychotic drugs *have* to be therapeutic—lest their forcible administration be transformed from treatment into torture; and schizophrenia *has* to be a brain disease—lest the medical legitimacy of psychiatry itself be undermined. □



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IDEAS ON LIBERTY
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# Capitalism and the Weak

*by Daniel Hager*

One allegation about capitalism is that it enables the strong to crush the weak. Some critics contend it models the ruthlessness of biological Darwinism's extermination of the weak through natural selection. In the Marxist view the entire proletarian class is enchained by the power of capitalists and must seize for itself the ownership of the means of production.

In reality capitalism *strengthens* the weak. Under capitalism the weak gain a degree of power not possible through other economic systems. One definition of capitalism is that it is a network of weaklings who combine their limited strengths to produce the unique personal power that accrues through abundance.

A vivid example of the strength of the weak under capitalism can be seen by considering the green seedless grape. This fruit has become such a staple in American supermarkets that its presence is no longer regarded with amazement. The domestic product is grown primarily in California. It is perishable. Yet it is available even 2,000 and 3,000 miles from there in top condition.

Another marvel added in the past two decades is that green seedless grapes are in supermarkets virtually year round even though California is a limited-source region in winter. Supplies have to come from some place where the weather is warm then, that is, the southern hemisphere. Chile produces most of the grapes marketed in the winter in North America. This highly perishable product reaches the stores after a journey of as much as 6,000 miles. Astonishingly, the volume is so plentiful that even the nonwealthy can consider a purchase.

Typically the American retail price per pound for green seedless grapes during the peak of the Chilean shipping season ranges from about $1.49 to $1.89 but lower during promotions. Based on a volume of 80 to 100 or more grapes per pound, depending on fruit size, the general non-sale price may be pegged roughly at two cents per grape.

The consumer who considers a purchase at that price is the weakest participant in the chain from vineyard to table. Most of us, if confronted with the challenge of securing green seedless grapes in February, would hardly know where to begin. One option would be to fly to Chile, buy grapes from a grower, arrange for shipment, then return home. The cost would be too high even to consider such a tactic. Yet, weak as we are, we have the power in the supermarket to decide either to buy grapes at only two cents each or to reject the retailer's offer.

Those elsewhere in the network are also weak. The grower may know how to grow grapes but falters at other points. He does not even have the strength to produce his crop without help from others. Mildew has been destroying grapes since at least the Old Testament times of Amos 4:9, and insects

*Daniel Hager (fris@michcom.net) is a freelance writer in Lansing, Michigan.*



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and other diseases also need to be controlled. The grower requires pesticides that he is incapable of making himself. Fortunately pesticide manufacturers have created products to save his crop.

Those in the pesticide companies are also weak. None probably could grow grapes well. Many pesticides are synthesized from petrochemicals, but the pesticide formulators would likely not know how to secure the raw product, to explore and drill for it, and then refine it after pumping up a supply. Similarly, the company that does obtain the petroleum is no doubt too weak in skills to convert it into a form that kills fungi and bugs.

The grape grower manifests another weakness after harvest. He lacks the competence to sell his crop to end users. However, an exporter helps him out and starts the process by arranging to ship a load overseas. But once it is at the foreign port, the exporter is probably too weak to move it onward. The North American market for fresh fruit is dynamic and complex, and the load needs the aptitude of somebody who has close contacts with multitudes of buyers and grasps changes in market conditions immediately. So a sales agency or broker takes charge of the load and makes a sale to a chain store, a terminal-market wholesaler, or a foodservice distributor.

But the product still needs to reach the buyer, and that seller, for all his knowledge about markets, is too weak in transportation skills to get it there. He has to engage the services of a truck broker, who secures a truck and driver, and through their efforts the grapes reach the proper destination.

## More Weak Links

The entire transportation process exposes the weakness of all who have a role in it. The truck broker and trucker do not have the strength to grow or import or sell the grapes, nor do they know how to build the truck or create the fuel to move it. The ship captain is likewise probably incompetent in the fruit business and is also doubtless unable to buy and own the ship. The ship owner because of his own weakness has to rely on others to build it. The builder of the ship is not strong enough to mine ore and smelt it into the steel that is fabricated into the ship.

Since grapes must be held at about 32 degrees Fahrenheit to prevent deterioration, constant refrigeration is required for the full journey from harvest to retail. Those directly involved in moving the load by sea or over land are likely unqualified to design, install, and maintain cooling equipment. Another essential is temperature recorders to track cooling failures if they occur. The manufacturer of these recorders knows how to build them but not how to create the plastic, metal, and silicate out of which they are assembled.

Making green grapes available to American consumers is a capital-intensive process from start to finish. Those who engage in it are too weak to command capital except in very restricted modes. If the retailer sought capital to build a fleet of ships, he would be rejected. If the truck broker requested capital to buy refrigerated seagoing containers, he would be turned down.

Each participant in the network is shackled by weakness. All each can do in response is concentrate on what he believes he is good at and what he can persuade capital providers is his skill. He is driven by a desire for personal profit. He tries to figure out how he can fit into the system to achieve it.

The success of capitalism derives from its grassroots nature. No central coordination exists. The system develops spontaneously from the ground up rather than by command from the top down. The participants engage in it voluntarily in pursuit of improving their own lives.

This is capitalism's strength—that there is nobody who is strong enough to be in charge.

Contrast other systems. Suppose a group, impelled by a sense of compassion, desired to provide the masses with a regular supply of seedless green grapes at a price of only two cents each. Out of its benevolent spirit it would offer to cover costs above the two-cent threshold should there be any. A pro-



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gram would be set up to effect the plan. Somebody would be chosen to direct the program.

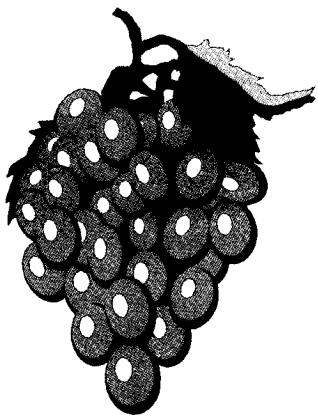
It would likely founder. The efficiencies imposed by the discipline of the marketplace would be missing. The subsidies required to sustain the program would likely balloon beyond the tenable. "Good works" would be unable to accomplish the good achieved by a spontaneous network of volunteers seeking personal gain.

Marxists insisted they had a system superior to capitalism and got a chance to learn about top-down control by the strong after Bolsheviks seized power in Russia in 1917. A series of failed economic one-year plans from 1924 onward culminated in the grand *Piatiletka,* the Five-Year Plan of 1928. The central State Planning Commission, explained fisheries expert Vladimir V. Tchernavin, determined "every conceivable detail" of the economy, producing "multitudes of tabulations by which it was possible, for instance, to see where and how much roofing iron, shoes, caviar, horseshoe nails, tractors, wheat, pork, eggs, milk, butter, fish, and so on would be produced and also how they would be used at any given moment of the Five-Year Plan."[1]

The system's intrinsic frailty was that a departure from quota for any one element would destabilize everything else like tumbling dominoes. An extra large catch of fish would, in the absence of market signals and spontaneous market responses, confront an inadequate preset supply of salt, so the surplus fish would rot. "Any deviation [from quotas], whether over-fulfillment or the opposite, in any given industry, would necessarily cause disruption. . . . So it was that, instead of the working out of an orderly plan, chaos prevailed."[2] The strong who managed the system turned into panicked weaklings whose primary occupations became the protection of their own backsides and a search for scapegoats.

Capitalism works the other way around, by making the weak stronger. Louis XIV was in his time the strongest man in Europe, the embodiment of the full power of the French state. But despite that strength he could not command the appearance of out-of-season grapes. Thanks to capitalism, being an ordinary American is better than being the king. □

1. Vladimir V. Tchernavin, *I Speak for the Silent* (London: Hamish Hamilton, 1935), p. 22.
2. Ibid., p. 23.





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IDEAS ON LIBERTY
MAY 2002

# Farm Frolics

*by Scott McPherson*

"Democrats love capitalism," charged U.S. Senator Phil Gramm of Texas during last year's debate over tax cuts, "but they hate capitalists."[1] It is fair to say that Gramm's analysis is on target—if only he would admit the corresponding truth in his criticism: that Republicans love capitalists but hate capitalism—particularly when it comes to their farming constituencies.

In what will surely be the biggest non-debate of many election-year "battles," Senate Republicans like Kansas's Pat Roberts are promoting more and more subsidies to farmers as crop prices fall. Prices for wheat, corn, cotton, and soybeans all plummeted in the late '90s, and have yet to recover. In response, Congress has approved four bailouts for the farm industry since 1998, to the tune of $28 billion.

Now, as several farm-state senators face re-election in what pundits are predicting to be close races, the government gravy train is once again at full speed. Currently Congress is working on an expansion of farm subsidy programs that would have the government making direct payments to farmers when prices are down. If this legislation fails to pass, however, "Congress will provide another round of supplemental assistance for farmers," the Associated Press reported.

*Scott McPherson (mcpherson0627@juno.com) is a freelance writer in Fairfax, Virginia.*

Though Republicans love to wax eloquent about the independent, virtuous, struggling businessman who pulls himself up by his bootstraps to build a dignified life on the products of his own toil, their professed love of free enterprise seems to ultimately depend on farmers' being immune from the process. What this amounts to is a love of the symbolic capitalist, accompanied by an unhealthy misunderstanding of what capitalism really means.

There is no reason why farming should be exempt from market forces and require the constant largess it now receives from the taxpayer. The most popular argument against ending farm assistance is that it will reduce the number of farms and create a situation like that of the breakfast cereal industry, which is dominated by a few large conglomerates. Looked at from any economic perspective, however, this is purely a red herring.

First, politicians' claims that subsidies are "necessary" to "protect" small farms from massive corporate takeover are largely exaggerated. E.C. Pasour, Jr., professor of agriculture and resource economics at North Carolina State University, writes that "two-thirds of government payments go to the wealthiest 15 percent of U.S. farmers."[2] This fact clearly discredits the teary-eyed sentimentalities of many subsidy supporters.

Second, if most farms in America were in fact to fall under the ownership of a few big



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companies, it is erroneous to think this would hurt consumers and farmers. For example, while technological developments in the textile industry in the early nineteenth century did cause short-term worker displacement, by the end of the century mills were actually employing *more* people than had previously worked in that field. This is due to the economic law of capital accumulation—businesses that are allowed to make large profits tend to reinvest their proceeds, fueling expansions that require more workers. Those farmers who cannot find work in the new environment will most likely be employed in those industries that boom with a fresh influx of funds, freed up from the wasteful spending that previously went to agriculture.

## Consumer, Have No Fear

Nor would consumers have anything to fear from such a development. The decline of mom-and-pop stores has yet to bring about the huge price hikes that many anticipated; it was precisely because large chain stores and supermarkets were charging *less* that they won the smaller stores' customers to begin with. The only thing that increased was the quantity and selection of goods on the shelves. If the farm industry were allowed to so effectively weed out its least productive, least efficient, and least profitable members, food prices would fall even more.

Like any other endeavor, farming will have both winners and losers. The role of the winner is to demonstrate the profitability of wise thinking and careful investment; his success means more people get more goods. Democrats seem to despise the one among many who succeeds and grows rich. On the other hand, Republicans want all farmers to be icons of capitalistic achievement, at the expense of the free market they claim to support. □

1. Michael Graczyk, "Gramm brings Bush tax cut campaign to home turf," Associated Press report in the *Abilene Reporter-News*, February 17, 2001.
2. See "Government should support agriculture—the backbone of America," in Mark Spangler, ed., *Clichés of Politics* (Irvington-on-Hudson, N.Y.: Foundation for Economic Education, 1996), p. 218, also posted on www.cliches.org.


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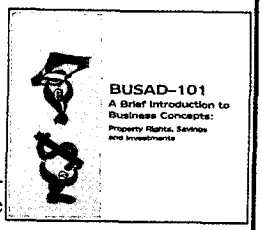


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IDEAS ON LIBERTY
MAY 2002

# The Perils of Populism

*by Christopher Lingle*

Populist policies that promote divisions between rich and poor sow the seeds of social instability and economic destruction. Zimbabwe's economic crisis and recent demonstrations can be traced directly to the rhetoric of populism used by the current government.

In the first instance, basing public policy on populism creates false expectations among the poor that cannot be fulfilled. When public officials suggest that poverty can be decreased or that social justice will be served by taking from the rich or by passing laws to raise wages, it provides the poor with a sense that their condition can and should be legislated away.

Consequently, populism tends to lead to expectations that the government will and should pursue policies of redistribution without rest until there is an egalitarian distribution of income and wealth. In response to these signals, it is understandable that the poor continue to demand to be given more by the government as a right arising from their identity within a group.

Constructing a system of group rights is fraught with danger. A government that pursues populist support by basing rights on economic or social characteristics is flirting with the destruction of the rule of law.

Indeed, the assertion of group rights over individual rights supported the injustices of apartheid in South Africa and genocide in other parts of the world. It reinforces a divisive mentality of "them and us."

As it is, the poor feel justified in expressing their grievances through street demonstrations to remind the government of its promises. The resulting chaos and hysteria of social unrest are the wages of the sin of populism.

What of those who supported the government's legislative mandate to raise wages? Those who believed that wages could be dictated by political legerdemain should not be blamed if they seek to push for an hourly wage of $100 an hour! After all, supposedly responsible people encouraged them to believe in that fairy tale.

And so, populism promotes the misleading idea that income and wealth redistribution can reduce poverty. On the contrary, poverty is the result of low economic growth because of insufficient capital formation. Poverty in Zimbabwe, as in many other emerging market economies, continues to be problematic because of government policies that hinder private investment.

A better approach to poverty reduction would be to remove barriers against legal activities that create employment. One of the lessons of the global economy is that only private initiatives can create sustainable economic growth and employment. Long-term investment by entrepreneurs will be stunted if there is a fear of capricious actions of

*Christopher Lingle (clingle@ufm.edu.gt) is a professor of economics at Universidad Francisco Marroquín and author of* The Rise and Decline of the Asian Century.



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a government that is running a populist agenda.

It's bad enough to halt new investment. But populism further undermines risk-taking associated with starting new businesses because it introduces additional uncertainty by increasing the probability that successful commercial ventures are subject to appropriation through political action.

A dilemma arises in explaining the politicians' populist rhetoric. It would be uncharitable and probably wrong to assume that it is stupidity on their part. That conclusion would also cause despair concerning their ability to resolve the current economic crisis. But is it better if they are motivated by a deep cynicism whereby they know better but hope that their potential supporters do not?

In the end, it is likely that the government suffers from a combination of cynicism with a strong dose of ignorance. (Ignorance reflects the lack of information, while stupidity is the inability to make sense out of information.)

This is evident in that some members of the Zimbabwe Congress are on record blaming globalization and other outside forces for the crisis. Such a ridiculous notion is only understandable when one considers that politics is the art of taking credit for the good and shifting the blame for the bad.

Instead of faulting globalization for their woes, Zimbabweans and most poverty-stricken citizens of the world should realize that their economies suffer from failures of governance. Poor policy decisions are being made within an increasingly defective "institutional infrastructure" that leads to frustration on the part of investors seeking evidence of growth potential.

## Role of Government

At issue is nothing less than the role of the state. Should this be a country of free individuals living under a general law guided by a permanent constitutional order? Or should it be destroyed by the chaotic interference of the capricious interpretations of a transient group of politicians?

The most basic role of a constitutional democracy is to provide a framework of law defining the limits of actions of individuals or groups in exercising their freedom of association and contract. All individuals should find dignity in their identity within any community they wish as long as those communities do not violate the rights of other individuals. However, membership in such groups should never accord them special privileges from the state. All individuals should be treated equally with no positive or negative discrimination among individuals in apparently similar situations.

It is an egregious error to encourage differential treatment on the basis of ethnicity or religion or class by imposing social engineering or unjustified confiscations. People should not be treated or monitored in accordance with what they demand or are said to deserve on the basis of some community or group status.

In sum, populism is a dangerous and destructive game that serves the narrow interests of those who seek to capture or preserve political power. The beneficiaries from such policies enjoy short-term gains of public office while shifting the burdens in the long run onto the poor who are deluded into supporting them. □



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Economics

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MAY 2002

# Public Interest or Private Interest?

That private interest dominates market decisions is widely accepted, if not always applauded. Farmers don't get up early on cold mornings in Nebraska to plant crops because of concern over world hunger, but because they want more income for themselves and their families. People don't invest in pharmaceutical firms because they want to help the sick, but because they believe those investments will increase their retirement incomes more than will alternative investments.

Farmers and investors occasionally claim that feeding the hungry and curing the sick provide much of their motivation, and certainly people do feel good about contributing to the well-being of others. But who doubts that if farm incomes and pharmaceutical profits dropped sharply, there would be fewer farmers plowing the fields and fewer dollars invested in medical research, regardless of the sickness and hunger in the world? The advantage of market economies is not that they motivate people to sacrifice their private interest for the public interest, but that they motivate people to pursue their private interest in ways that best promote the public interest.

On the other hand, government decisions are commonly thought to be motivated by noble social concerns like helping the poor, protecting the environment, improving education, and promoting economic growth. Of course, government decisions are made by people, just as market decisions are, but supposedly when people move from market roles to political roles they experience a moral metamorphosis, discarding their private interest to better promote the public interest. Serious people would acknowledge, if confronted with the issue, that no such metamorphosis occurs, yet the view that political officials care deeply about us and our problems is remarkably common.

A far more accurate, and useful, perspective on political decisions is that they are motivated by private interest just as market decisions are. True, people often vote for policies, or candidates who support those policies, on the basis of public concern, but that can be explained by the minuscule probability that any vote will affect the outcome of an election. So voting is a great way to feel socially concerned at low cost. (I discussed this "expressive voting" last month.) If voters were really willing to sacrifice for public benefit, they would make sure the money spent by the programs they favor accomplished their stated goals. But that would be costly. Having voted to "do good," few voters ever know whether any good is actually done.

But because every government program affects politically organized groups, these groups do follow up on how programs are designed and implemented. And because the political influence of these groups is significant, their members make sure that government programs serve their private interest, even when this means doing less to accomplish noble public objectives.

*Dwight Lee (dlee@terry.uga.edu) is Ramsey Professor at the Terry College of Business, University of Georgia, and an adjunct fellow at the Weidenbaum Center on the Economy, Government, and Public Policy at Washington University in St. Louis.*



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The best evidence on who benefits the most from government programs supposedly dedicated to worthy public objectives is to consider the following two questions. First, can government best accomplish desirable social goals by downsizing bureaucracy and reducing transfers and privileges to an organized interest group? Second, can you think of a government initiative to accomplish a desirable social goal that downsized a bureaucracy or reduced transfers and privileges to an organized interest group?

The answer to the first question is clearly yes, as we are about to see. The answer to the second question is, it's difficult. I can think of very few examples. The elimination of the Civil Aeronautics Board, the Interstate Commerce Commission, and the military draft are possible examples, and I challenge readers to come up with additional examples and e-mail them to me. With few exceptions, when governments attempt to accomplish a public benefit, they undermine the attempt by making sure that the interests of politically influential groups (including government bureaucracies) are well served. This means that, if public authorities were seriously concerned with promoting the public interest, there would be lots of ways they could do so much more effectively by reducing spending and special-interest privileges. Don't hold your breath.

## Doing Good by Doing Less

Politicians have so persistently expressed their deep desire to help the poor, and their belief that only government can provide that help, that many Americans now believe that without the federal government, masses of poor people would be starving in the streets. But removing all import restrictions and eliminating all agricultural price supports would do more to help poor Americans (by lowering prices) than all the social-welfare programs combined. Welfare programs have done little, if anything, to alter the distribution of income; instead they have reduced economic growth, thus probably leaving the poor worse off.

As I discussed at length in previous columns, we could do more to protect the environment, and do it more cheaply, by shifting from command-and-control to market-based policies to reduce pollution. But doing this would greatly reduce the budget and power of the Environmental Protection Agency and remove protections against competition that current policies provide to politically influential businesses and labor unions—such as those involved in mining eastern coal.

Politicians never tire of stressing the importance of improving the education of our youth and promising meaningful education reform. Yet simply giving students and their parents educational choice would do far more to improve education in America (particularly for children in the poorest neighborhoods) than all the money spent by the U.S. Department of Education and all the methods courses taught in college education departments combined. But allowing parents to make schools compete for their dollars by providing better education at lower cost would destroy the control of politically powerful teachers' unions and undermine the rationale for thousands of bureaucrats.

If the federal government really wanted to promote economic growth, it would eliminate our impossibly complex tax code and replace it with a far simpler tax with one low rate on income and few, if any, exemptions. The tax system can never be quite as simple as some suggest, but it can be far less complicated and do far less to distort economic decisions and reduce economic growth than our current system. But with a simple tax system, politicians would lose their power to provide (read sell) special-interest tax breaks, and hordes of lobbyists, tax accountants, lawyers, and employees of the Internal Revenue Service would have to find more productive work.

There are many more examples of how governments, if they really were motivated to promote noble social goals rather than serve the private interest of the politically influential, could accomplish more by doing less. As my friend—and well-known economist—Murray Weidenbaum likes to tell government authorities, "Don't just stand there, *undo* something." □



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IDEAS ON LIBERTY
MAY 2002

# Race, Culture, and the "Digital Divide"

*by Larry Schweikart*

Prior to the September 11 attacks and the stock market slump, one of the hottest policy issues debated by technology scholars was the so-called racial "digital divide," a term concocted to portray "haves and have nots" in the world of the Internet. The paper "Bridging the Digital Divide: The Impact of Race on Computer Access and Internet Use" is typical: "[S]ome social scientists are beginning to examine carefully the policy implications of current demographic patterns of Internet access and usage."[1] Former Vice President Al Gore suggested several policy proposals for closing the "digital divide," and President Bill Clinton's "Call to Action for American Education" proposed universal Internet access for students.

Studying race or group behavior is dubious at best; in today's climate, it's even dangerous, since racial groupings are used by collectivists to serve a political agenda. Nevertheless, it is useful to examine the claims being made. Thomas Sowell has cautioned that culture, for example, is a far more important factor in economic activity than race, and in the case of the digital divide, the "experts" may be examining racial characteristics when they should be considering cultural effects. There is also substantial new data showing that Americans are racially intermarrying more frequently. The Census Bureau threw up its hands in frustration trying to count mixed-race Americans in the last census.

That said, let's examine the new arguments about the digital divide, pretending for a moment that race was a factor in computer access and use.

First, although many readers may have trouble recalling a time without computer technology, it is still relatively new. Nevertheless, the Internet has filtered through the social strata from the top down faster than any other technology in history. According to Joel Kotkin and Ross DeVol's working paper for the Milken Institute, here is how fast selected products spread to 25 percent of the population:

| Product | Year Invented | Years to Spread to 25 percent of Population |
|---|---|---|
| Electricity | 1873 | 46 |
| Automobile | 1886 | 35 |
| Radio | 1906 | 22 |
| Television | 1926 | 26 |
| Cellular Phone | 1983 | 13 |
| Internet | 1991 | 7 |

Joel Kotkin and Ross C. DeVol, "Knowledge-Value Cities in the Digital Age," Milken Institute Study, February 13, 2001, p. 2.

Internet usage in 2001 reached 176 million Americans, 62 percent of the population, according to one Nielsen survey, up

*Larry Schweikart (schweikart@erinet.com) teaches history at the University of Dayton.*



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from 57 percent just a year earlier. Still, "digital dividers" sound the alarm. Jesse Jackson claimed that differences in Internet use between whites and blacks are "classic apartheid."[2] Research shows that differences in Internet use have little to do with income. Instead, computer access has played the pivotal role, according to Thomas Novak and Donna Hoffman of Vanderbilt University.[3]

To solve the "problem" (with "problem" defined as any differences between groups), obviously all the government needs to do is to make sure that regardless of income, everyone has access to a computer.

Not so fast. Other evidence shows that blacks in high numbers have computer access at work—virtually equal to that of whites—and that if one holds income and education constant, blacks are *more likely* to have computer access at work than whites.[4] This statistic makes sense considering that blacks, in far higher proportions than whites, work for state, local, or the federal government, where computers are provided.

Does education explain the "divide"? There appears to be a link between education and computer access, but a tenuous one. Both British and American studies have shown that more highly educated people tend to use the Internet more, although the notion that pinheaded "friendless nerds" comprise the majority of "surfers" is baseless: one U.K. study found that "internet users lead more sociable lives than non-surfers."[5] However, before researchers jump the gun to claim a link between education levels and Net use, existing studies would have to go much further to hold constant the *quality* of education in racial comparisons, something that is seldom done.

## Divide Myth

When the rhetoric is stripped away, it appears that the racial "digital divide" is largely a myth, and to the extent it does exist, it is somewhat correlated to education and somewhat correlated to access to computers. Aha, say the "digital dividers," maybe racial groups don't have equal access to computers.

Computer access can mean having a computer at work or at home, but researchers have tried to argue that having access *only* at work won't cut it. Where a sharper divide occurs is in home computer ownership; 44 percent of whites have access to home computers compared to 29 percent of blacks. For this reason, at least one study claims, whites are more likely to use the Internet for information on a regular basis.[6] Net-use rates correlate to having a home computer *and* a computer at work. The Vanderbilt study found that this was just about the only instance in which "race matters"—when students lacked a computer at home. "White, but not African American students," wrote the researchers, "are able to take advantage of non-traditional access locations including homes of friends and relatives with home computers, and libraries and community centers with Internet access."[7] Even so, the study admitted more blacks were on line than is popularly thought and that the number was growing. As blacks became more familiar with the Internet, the authors concluded (apparently somewhat glumly), they would "catch up" to whites.

These findings pull the rug out from under the advocates of government provision of computers "access" through schools and public facilities. The key is not "access," but *attitude*. Clearly, having access to public education did not close the "education gap." Access to income-maintenance and welfare programs did not close the "income gap." And now, with large numbers of computers at schools and public facilities, the researchers claim (surprise!) that free computers in public settings have not significantly closed the "digital gap." Of course, to some extent, big-government types will use these studies for the perverse claim that we need to provide computers to low-income people in their homes. Indeed, in supporting tax-funded computer access for the homeless, the Digital Divide Network claimed that "Americans have long agreed that certain communications tools are so fundamental that their provision should not be left to the vagaries of the marketplace alone."[8]



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## Cultural Differences

The "digital divide" involves cultural differences and experience levels that no government policies can address. For instance, another Vanderbilt study "found interesting differences in media use between whites and African Americans that also deserve further probing. For example, although the rate of home PC ownership among African Americans is flat or even decreasing, their rates of cable and satellite dish penetration are increasing dramatically. At a minimum, our results suggest that African Americans may make better immediate prospects than whites for Internet access through cable modems and satellite technology."[9]

A British researcher found that there is a "huge divide" between those who surf the Net and those who do not. They differ in many respects, including income and education. Moreover, surfers "simply watch less television."[10] Once again, the "experts" are in a quandary, because as far as I know, races don't demonstrate broadly different patterns of television viewing—some, to be sure, but even then, further analysis of the data points back to cultural, not racial, differences.

Are there differences in *how* races use the Internet? A broad study done in August 2000 by the Pew Internet & American Life Project, found significant differences in Net usage between blacks and whites. For example, blacks were 69 percent more likely than whites to have listened to music online, 45 percent more likely than online whites to play a game, and 12 percent more likely to "browse just for fun." They were also nearly 40 percent more likely to have looked for information about jobs online and 65 percent more likely to seek religious information. But whites were slightly more likely to obtain financial information, and they purchased more products over the Internet.[11] However, the races were approximately equal in their use of the Net to get political news or information.

Contrast white and black use of the Web with Asians, who obtain news from it at an even higher rate than whites, download music more often than blacks, and get political information more often than either blacks or whites. Asians are also more likely than blacks to search for jobs and conduct work-related research on the Net, or to buy or sell stocks online than whites. They are, however, less likely than blacks to search for health information or listen to music online.[12]

The implications of these findings suggest trouble for those who think they can eliminate whatever "digital divide" that may exist through government programs. Buried in these studies is evidence that the members of racial or ethnic groups use the Internet differently—whites more for business and product purchases, blacks more for entertainment and spiritual growth, Asians for work research and political news.

That the patterns of technology use across racial and ethnic groups are not uniform should come as no surprise. Sowell has pointed out that ethnic groups have had different paths to economic success. He has documented the propensity of the Irish, for example, to dominate police and fire departments in eastern urban areas, seeing those jobs as a path to social acceptance and stability. On the other hand, Lebanese, coming from a commercial background, disproportionately go into grocery businesses, and blacks have disproportionately entered government employment and opened auto dealerships. Asians have focused on mathematics and engineering more heavily than other groups.[13]

One use of the Internet is not necessarily better than another—but there are clear differences that would manifest themselves in income, much the way a person who used his car to haul goods would have a different return on his vehicle from someone who polished it up for car shows on the weekend.

## Market Bridges Divide

The fact is that the free market has moved rapidly to span the "digital divide" by making technology more accessible.[14] Computers have become so inexpensive that almost anyone can own one, and Internet access is also



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cheap. What critics of the "digital divide" do not grasp is that people make choices about their resources. Of course, people will accept a free computer . . . or a free television, or a free Thanksgiving turkey. But when pressed to spend their own money on goods or services, it becomes clearer what aspects of their lives people value most. Unless the big-government advocates are ready to start regulating the number of hours that people watch television, the state can hand out computers like free movie passes without any impact on incomes.

All that minority groups need to finish bridging the "digital divide" is to gain further hands-on experience, which will come as younger generations learn the tools of the computer age. There are also work habits that must be adopted if the Internet is to assist in wealth creation. But acquiring them in cyberspace is no different from learning them at McDonald's. Once these habits are established, the benefits of Internet access can become fully realized.

One cannot, however, ignore the implications of using the Net more for entertainment than for work. It is almost a given that the next generation of computer-related products will be in the realm of the "telecosm," George Gilder's name for the ethereal world of data in the telecommunications networks.[15] Gilder has argued that computers themselves will become less important and valuable as more information, and even operating systems, are stored on the Net and downloaded as needed. If that is true, what counts are skills, not hardware. And if Gilder is right, there will be more distractions than ever on the Net, requiring more discipline to block out entertainment and to bore in on wealth creation.

In short, racial aggregates may indeed have different use patterns when it comes to the Internet, but these are largely attributable to different cultural emphases. If this constitutes a "digital divide," so be it. But do we really want government to dictate our Internet habits? Different people have different views on how best to use the Internet. When the call for "equal access" to the Net proves insufficient to change people's perceptions about how they value their online time, will we next hear calls to "train" people to use the Internet in "preferred" ways? Let us hope that the freedom enabled by the telecosm prophesied by Gilder does not become another tool to divide the races. That would truly be a disastrous "digital divide." □

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1. Thomas P. Novak and Donna L. Hoffman, "Bridging the Digital Divide: The Impact of Race on Computer Access and Internet Use," February 2, 1998, working paper available at wwww2000.ogsm.vanderbilt.edu/papers/race/science.html, and published as "Bridging the Racial Divide on the Internet," *Science*, April 17, 1998, pp. 390–91. References here are to the Internet version.

2. Quoted in Adam D. Thierer, "How Free Computers Are Filling the Digital Divide," *Heritage Foundation Backgrounder*, No. 1361, April 20, 2000, p. 2.

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4. Ibid.

5. Duncan Graham-Row and Will Knight, "Internet Users More Chic Than Geek," *New Scientist*, November 26, 2001, at www.newscientist.com/news/news.jsp?id=ns99991606.

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7. Ibid.

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9. Donna L. Hoffman, Thomas P. Novak, and Ann E. Schlosser, "The Evolution of the Digital Divide: How Gaps in Internet Access May Impact Electronic Commerce," available online at www.ascusc.org/jcmc/vol5/issue3/hoffman.html.

10. Graham-Row and Knight.

11. Tom Spooner and Lee Rainie, "African-Americans and the Internet," Pew Online Life Report, October 22, 2000, available at www.pewinternet.org/reports/toc.asp?Report=25.

12. Tom Spooner, Lee Rainie, and Peter Meredith, "Asian Americans and the Internet: The Young and the Connected," Pew Online Life Report, December 12, 2001, available at www.pewinternet.org/reports/toc.asp?Report=52.

13. Thomas Sowell, *The Economics and Politics of Race* (New York: William Morrow, 1983).

14. Donald L. Alexander, "Internet Access: Government Intervention or Private Innovation?" Working Paper, Mackinac Center for Public Policy, December 1999.

15. George Gilder, *Telecosm: How Infinite Bandwidth Will Revolutionize Our World* (New York: Free Press, 2000).



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IDEAS ON LIBERTY
MAY 2002

# Who Is a Liberal?

*by Jim Peron*

Liberals have it tough. I mean the real liberals. Not the modern watered-down socialists who call themselves liberals, but real, honest classical liberals. There is so much confusion over the term "liberal," and real ones have allowed fake ones to get away with this subtle destruction of the language.

Recently I was reading two different books from two different perspectives. One was J. Salwyn Schapiro's *Liberalism: Its Meaning and History*,[1] and the other was the *Suicide of the West* by the conservative writer James Burnham.[2]

I would assume that both these men were highly intelligent and that they wouldn't allow this purposeful distortion of the meaning of "liberal" to continue. I at least expected they would acknowledge how the term had been distorted and then explain what liberalism actually stands for. But they didn't. In fact, both of them supported this destruction of meaning.

After listing the libertarian principles of liberalism, Schapiro spoke of the evolution of liberalism into something entirely different. His readings on liberalism include works by Hegel, Bismarck, and Franklin Roosevelt. Schapiro seems to assume that simply using the label "liberal" is enough to make one a liberal. If a farmer had a herd of goats and named them Fido, Spot, and so on, these goats wouldn't suddenly become dogs. Yet Schapiro includes anti-liberals as liberals because these opponents of liberalism used the name to disguise their illiberal programs.

Burnham was even worse. His book is supposed to be a classic of conservative thinking. If this is true then I had no idea how bad conservative thinking is. Burnham argued that we can't know what liberalism is until we know who is liberal. He didn't mean who originated liberal thinking and what principles they held. He meant who was called a liberal at the time he wrote his book.

Behold his logic: "The plain commonsense fact is that everybody knows Eleanor Roosevelt was a liberal, just as everybody knows that Fido, who runs around the yard next door, is a dog. We all know that Mrs. Roosevelt was a liberal even if we have no idea what liberalism is. *Whatever* liberalism is, she was *it*. That's something we can start with" (pp. 28–29).

But neither Fido nor Eleanor was the first in their class. The category "dog" and "liberal" existed before either of them. And those categories had specific definitions by which both Fido and Eleanor could be judged. Let us assume that Fido had long skinny legs and a long neck, which was used to reach leaves from the top of trees. If I told you he was yellow and brown and spotted, you might point out that I'm not describing

*Jim Peron (peron@gonet.co.za) is executive director of the Institute for Liberal Values in Johannesburg, South Africa.*



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a dog at all but a giraffe. And calling that giraffe "Fido" won't change a thing.

Burnham seems to have had things backwards, and he calls this common sense. Fido is a dog because everyone knows he's a dog and not because he meets some objective criteria. And the illiberal Eleanor Roosevelt was a liberal simply because everyone knew it. Burnham then listed an honor roll of illiberal liberals to support his Roosevelt thesis. This is followed by his announcing that there are no clear-cut principles on which to pin the term "liberal." Thus it's a fluid term, but he had another common-sense way to decide who is or is not liberal.

Burnham listed 39 statements and said that liberals will agree with "every one, or very nearly every one" of them. A good conservative, of course, will disagree with nearly every one of them. But Burnham failed to recognize that many true liberals would probably agree with about half of his sentences.

Earlier in his book he said that a good nonliberal professor was Milton Friedman, though Friedman calls himself a true liberal. To judge Burnham's test for accuracy, I examined the statements from Friedman's point of view as best as I understand it. A few of Burnham's statements are confusing and hard to answer. But I calculate that Friedman would agree with about 15 of the statements. Yet as a nonliberal he was supposed to disagree with the overwhelming majority. There was something clearly wrong with Burnham's thinking.

## Freedom of Speech

Burnham, for instance, lists several statements that imply that liberals support freedom of speech and conservatives oppose it. Burnham's conservatives would oppose the following (pp. 40–42):

- freedom of opinion and expression;
- freedom of thought and conscience;
- equality of political rights without distinctions such as sex, race, color, birth, status, social origin, and so on; and
- respecting the religious beliefs of others.

And Burnham had good conservatives supporting the following:

- some racial segregation and discrimination;
- political, economic, or social discrimination based on religious belief;
- using "methods of torture and physical terror" during "political or military conflict";
- colonialism and imperialism;
- stripping communists of the right to express their opinions; and
- congressional investigating committees.

This list exposes Burnham's apparent ignorance of the tradition of classical liberalism. Burnham could not explain how many people can support free speech and oppose colonialism and torture, while still opposing mandatory unionism, socialized medicine, and equal-pay laws, also on his list. If Burnham's framework has no room for such people, the problem is with Burnham's framework.

He lamented that no books existed which explained what liberalism stood for "save for that one modest and rather superficial little volume by Professor Schapiro, whose name is not elevated enough to count very much on those loftier planes where our opinions are made and remade" (p. 144). Two centuries of liberal writing were ignored so that Burnham could prove his point. But even with the faults previously mentioned, Schapiro's book gives some excellent explanations of liberal principles.

Here are some of the basic tenets of liberalism, according to Schapiro:

- "What has characterized liberalism at all times is its unshaken belief in the necessity of freedom to achieve every desirable aim. A deep concern for the freedom of the individual inspired its opposition to absolute authority, be it that of the state, of the church, or of a political party" (p. 9).
- "Liberalism has proclaimed the principle of equality for all human beings everywhere. It must be borne in mind, however, that equality does not mean that all have equal ability, or equal moral perception, or equal personal attraction. What it means is that all have equal rights before the law, and that all are entitled to civil liberty" (p. 10).
- "In the liberal view the chief end of government is to uphold liberty, equality and security of all citizens." Schapiro says that



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government must respect the rule of law, that all power rests on the consent of the governed, and that "liberalism has placed highly important limitations on the power of government" (pp. 10–11).

• "Of all civil liberties, the most prized has been liberty of thought and expression" (p. 11).

• "The stress placed by liberalism on intellectual freedom derives from the conviction that man is essentially a rational creature—not indeed that he is always reasonable, but that he has the faculty of being so" (p. 11).

• Since liberalism was fundamentally rationalist it viewed religion from a secular perspective advocating freedom of religion but the separation of church and state (pp. 11–12).

• Liberalism, because of its secular perspective, "adopted a dynamic view of life, envisaging progress for mankind" (p. 12).

These ideas can, of course, be found in the writings of such great liberals as Thomas Jefferson, Frédéric Bastiat, Richard Cobden, Adam Smith, John Locke, Herbert Spencer, Ludwig von Mises, and others. Since it is clear that Burnham had read Schapiro, he should be able to define a liberal fairly accurately even if he had stopped reading after 13 pages.

With this in mind one can easily refute Burnham's common-sense view. Eleanor Roosevelt did not hold to equality before the law but to equality of results. She did not advocate a limited government that had as its prime function the defense of liberty. And just because you've named your pet giraffe Fido that doesn't make it a dog. □

1. J. Salwyn Schapiro, *Liberalism: Its Meaning and History* (New York: Van Nostrand Reinhold Co., 1958).

2. James Burnham, *Suicide of the West: An Essay on the Meaning and Destiny of Liberalism* (New York: The John Day Company, 1964).

**OOPS! We Can't Find the Government!**

Princess Navina has spent her young life studying the governments of other lands, but in Voluntaria she draws a blank. Reacting against their history of past violence, the people of Voluntaria have sworn off using force to manage society. As a result, they have none of the political fixtures of the modern world: no taxation, no regulation, no laws... and no lawyers!

How do they solve the problems of daily life without depending on politicians? The solution is so simple one wonders why no one has thought of it before.

Political scientist Jim Payne, the creator of the Princess Navina series, has written fourteen books on topics ranging from the Peruvian labor movement to the U. S. Congress. "After 41 years of research," he says, "I think I've figured out what's wrong with government and what we can do about it. I've put the answer in fictional form to engage youthful minds without distressing elderly ones."

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# The Dreaded "D" Word

*by Christopher Mayer*

Deflation is a much-feared economic phenomenon, perhaps because it is most often associated with the Great Depression of the 1930s or with the recent troubles in Japan. And yet deflation has not always been coincident with periods of depression.

The general record of the nineteenth century, in sharp contrast to that of the twentieth, was one of falling prices, which Murray Rothbard called a "wonderful long-run tendency of untrammeled capitalism."[1]

The gold standard had the effect of suppressing large sustained increases in the money supply. Therefore, even after inflationary spikes, such as during the War of 1812 and the Civil War, deflationary busts soon followed, which checked long-term increases in prices.

Furthermore, as economist Marc Faber noted in a recent essay, "while the entire 19th century was characterized by a deflationary trend (commodity prices and interest rates in 1900 were half those of 1880), it was a century during which enormous economic progress took place accompanied by strong population growth."[2] Real wages rose dramatically during the nineteenth century, global trade flourished, and manufacturing capabilities improved.

Deflation, it seems, is largely misunderstood. What causes it? Is it happening now? A brief exploration into the nature of deflation might be helpful.

Deflation, like its sibling inflation, is properly defined as a monetary phenomenon. Yet rather than fight that battle over semantics here, the popular definition will suffice for purposes of this piece. Deflation is popularly defined as a condition where prices are generally falling. It can also be defined as a contraction of the money supply, which tends to lower prices as well. Stated another way, in a deflationary environment the purchasing power of money generally increases. This is the opposite of inflation, where the purchasing power of money generally falls, a condition post-World War II generations know well.

As Ludwig von Mises insightfully observed, there is always either inflation or deflation.[3] The purchasing power of money is not stable, but responds to the tugs and pulls of economic forces constantly acting on it. There are unavoidable continuous fluctuations, sometimes small and subtle.

Just as inflation punishes some (savers) and benefits others (banks), a deflationary environment likewise produces winners and losers. For example, deflation will inevitably make it tougher on some businesses that are unable to lower their expenses as quickly as their selling prices are falling. Contractual obligations—debt contracts, rents, labor contracts—all become a greater burden and make the downward adjustment hard on profits. As debts are extinguished and cred-

*Christopher Mayer (cwmayer@aol.com) is a commercial loan officer and freelance writer.*



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it contracted, bank profits are slashed. (As Mises wrote "credit expansion is a boon for the banks, contraction is a forfeiture."[4]) But, on the other side of the ledger, savers gain as their pool of savings increases in purchasing power. Fixed-income groups also benefit. And, as happened during the nineteenth century, real wages rise. Deflation does not automatically mean unemployment, as long as wage rates are not kept artificially high by government or labor union interference.

Which brings us to an important point. Deflationary forces can be either voluntary or compulsory. A voluntary deflationary push arises from the actions of free individuals and private firms in an economy. There are three ways that a free-market economy drives down prices.

First, there is the deflationary effect of increasing productivity and innovation. For example, as Faber points out, the "emergence of efficient trans-ocean steamships" and the opening of canals reduced transportation costs dramatically, which also had the wide-ranging effect of saving money and time, thereby improving the standard of living.[5] Other innovations in our own time also have deflationary effects; the power available in a desktop computer far exceeds what was available for similar money even ten years ago. This can sometimes be forgotten in a world where continuously expanding fiat money smothers these felicitous market outcomes.

## Demand for Cash

Second, deflationary effects may arise from an increase in the demand for cash. Thinking back to basic supply-and-demand economics, if the demand for something increases (in this case, money), its price (in this case, the purchasing power of money) will tend to rise, all else being equal. This form of deflation is particularly vilified among contemporary economists who believe that the best way to achieve prosperity is to spend money.

Finally, deflationary effects could be unleashed by a contraction of the money supply (including credit). Because the banks have inflated their assets during the boom, the natural process during the bust is to contract as businesses and consumers stop borrowing and pay back or default on debts, and as banks become more cautious, slowing or halting altogether the credit-creation process. Even so, this deflation has a limit. And that limit is, as Rothbard pointed out, "the eradication of all previous credit expansion."[6]

These deflationary causes are benign and corrective of previous excess. It is the compulsory or forced deflation that is the most damaging. The most popular way governments attempt to combat deflation is essentially to print money. Governments also attempt to create deflationary forces as a tool to combat rampant inflation.

Recently, Argentina froze more than a third of its people's savings to protect its banks and to attempt to salvage the purchasing power of the peso. "Since early December," a *Washington Post* article notes, "depositors have faced limits on withdrawals from savings and checking accounts."[7]

The government of Argentina, in an effort to curb the inflation it created by printing fiat currency, is now denying its people access to their savings. It is yet another abominable violation of property rights by a government, an outright theft perpetrated under the guise of saving the Argentine economy.

Freezing savings accounts is basically a way to force people to hold greater cash balances, a way to artificially prop up the demand for cash. As noted, an increased demand for cash is a deflationary force. In this case, Argentina hopes to harness it to defeat its opposite, inflation.

It is a story told countless times in the history of human affairs. As pointed out by Rothbard in his essay "Deflation, Free or Compulsory," such measures failed President Collor de Mello of Brazil in 1990 and they failed President Mikhail Gorbachev in the Soviet Union. It is hard to see anything but failure for such a policy in Argentina.



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## Deflation Now?

Some economists believe the global economy is susceptible to experiencing widespread deflation. Morgan Stanley economist Stephen Roach recently wrote, "for the world as a whole, I would judge the risk of deflation to be higher than at any point in 70 years."[8] Other observers already believe deflationary forces have kicked in, and point to the decline of commodity prices around the world.

Not everyone is on that bandwagon, however. James Grant's piece in *Forbes,* "What Deflation?," pointed to a rising median consumer price index and the continued expansion of the Federal Reserve's balance sheet.[9]

The inflation/deflation debate will probably continue. Part of the problem is, as Mises noted long ago, that the terms inflation and deflation lack "categorical precision" because whether a change in purchasing power is large enough to be called inflation or deflation involves some personal judgment.[10] Certainly, the measurement of such phenomena is a difficult if not impossible task.

Whether deflation occurs (or is occurring) is not the point of this essay. Deflation, as with all economic phenomena, will create opportunity for some and hardship for others. For perspective, however, we should not associate deflation only with periods of economic bust. Moreover, deflationary currents that arise from benign market forces created by the actions of individuals are corrective of a previous inflationary boom. Any hindering of this process can only cripple and delay a recovery. □

1. Murray Rothbard, "Deflation, Free or Compulsory," reprinted in *Making Economic Sense* (Auburn, Ala.: Ludwig von Mises Institute, 1995), p. 238.
2. Marc Faber, "Long Live Deflationary Shocks, and Down with the Central Bankers Who Want to Prevent Them," *Strategic Investment*, December 12, 2001, p. 10.
3. Ludwig von Mises, *Human Action: A Treatise on Economics* (Scholar's Edition) (Auburn, Ala.: Ludwig von Mises Institute, 1999), p. 419.
4. Ibid., p. 565.
5. Faber, p. 9.
6. Murray Rothbard, *Man, Economy, and State* (Auburn, Ala.: Ludwig von Mises Institute, 1993), p. 866.
7. "Argentina Freezes CDs," *Washington Post*, January 11, 2002.
8. Stephen Roach, "Deflationary Perils," *US and Americas Investment Perspectives*, Morgan Stanley, November 7, 2001, pp. 15–16.
9. James Grant, "What Deflation?," *Forbes.com,* December 24, 2001.
10. Mises, p. 420.

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Economics

# I Recycle!

I spoke recently to a group of college students on the economics of environmental protection. As I spoke of the market's amazing ability to conserve natural resources, one young man asked me, "Do you recycle?"

"No," I answered.

"Well, thanks for the effort," he replied with bitter sarcasm.

Before I could explain my answer, he gathered his books angrily and marched from the room. While no one else left, I could tell that most of the remaining students shared the sentiments of the student who had left. My talk's conclusion was awkward and unsuccessful.

Only later did I realize that I'd given the wrong answer. In fact, I recycle every day of my life!

Consider a typical day.

After I awaken, I shower and dry myself with a towel that I've had for a few years. I use this towel day after day. I don't discard it after one use. When it gets dirty, I toss it in the washing machine to clean it for further use. I recycle my towel.

Then I brew coffee and fix breakfast. Each day I use the same coffeemaker that I used the day before. I clean it after each use, recycling it for the next time. My wife and I drink the coffee from mugs that have been used many times in the past. (Actually, one set of our coffee mugs was handed down to us after my wife's parents used them for several years.) We also eat our breakfasts using dishes and utensils that are recycled from countless past uses. After breakfast, we don't throw our mugs, dishes, and utensils away; instead we put them in the dishwasher to be recycled for yet another use.

After breakfast, I dress myself in clothes that I've worn before and that I will wear again. My underwear, my pants, my shirt, my necktie, my belt, my coat, my shoes, my wristwatch—all are recycled from previous uses. And when I remove these clothes at day's end, I'll recycle them again, with the help of our automatic washer and dryer.

When my wife and I drive to work, we drive automobiles that we used the day before and that we'll drive for the next few years. We don't junk them after a single use. Instead, we recycle them, day in and day out.

The pots and pans that we use to prepare our meals—our toaster—our refrigerator—our television—our compact discs—our furniture—and, indeed, our house itself are all routinely recycled, use after use after use.

My family and I recycle a lot! And we're not alone. Everyone recycles a lot.

## Real Recycling

If I'd responded in this way to that student he probably would have asserted, "That's not recycling. Real recycling is re-using things that most of us think of as garbage."

That student, like most people, thinks of recycling as dealing with a handful of items

*Donald Boudreaux (dboudrea@gmu.edu) is chairman of the economics department of George Mason University and former president of FEE.*



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that are wrongly thought to be semi-precious: cans, bottles, plastic containers, and newspapers.

But why do I treat my clothing and dinner dishes different from my empty beer cans and day-old newspapers? The student who walked out on me sees that as a moral failing. I don't.

No moral issue turns on recycling per se. It might well be immoral to waste things, but contrary to popular misconception, failure to recycle is not wasteful. Real waste happens when someone recycles for the sake of recycling—that is, recycles without weighing its costs and benefits. If it is immoral to waste, then it is immoral to recycle when the benefits of doing so are less than the costs of doing so, because such recycling is wasteful.

We recycle as much as we do because it makes good sense to do so. It would indeed be wasteful for me to discard my fine china after each use. So I don't do it. And I don't do it because the market reliably tells me that it's wasteful to do so. I'm of no mind to purchase new china after each meal because the price of fine china far exceeds the value to me of the time I must spend cleaning and storing mine for future use. I'd quickly go broke if I refused to recycle most of the things that I regularly recycle. (Incidentally, I'll bet that even Bill and Melinda Gates recycle their fine china.)

But I do discard paper plates after each use. The reason, at bottom, is no different from the reason I recycle my china rather than discard it: it would be wasteful to do otherwise. After all, I *could* recycle paper plates. Careful washing would enable my family and me to reuse paper plates a couple or three times. But notice what would be wasted: valuable labor and time. One important reason for using paper plates would be undermined. That reason, of course, is the importance of saving the time and effort that it would take to wash dishes following the meal. Time that I could spend playing with my son, relaxing with my wife, reading a good book, or fixing a leaky faucet would be wasted cleaning paper plates. And to what purpose? None. Paper plates are so expendable precisely because the materials necessary to make them are so abundant. This abundance is reflected accurately in their low price.

The market prices resources accurately enough for us to be confident that if the materials used to make any items that are not now recycled become sufficiently scarce, the prices of those materials will rise. These higher input prices will raise the prices paid by consumers for these items, giving consumers greater incentives to recycle them.

Reflecting on the impressive amount of recycling that actually takes place daily casts doubt on the prevailing misperception that people are naturally wasteful and mindlessly irresponsible. In fact, market prices compel us to recycle when recycling is appropriate —and to not recycle when recycling is inappropriate. □

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# BOOKS

## Rebel Code: Inside Linux and the Open Source Revolution

by Glyn Moody

Perseus Publishing • 2001 • 334 pages • $27.50

*Reviewed by Andrew Morriss*

During the Microsoft antitrust trial a great deal of ink was spilled in the press over Microsoft's alleged monopolization of various markets and its practices in marketing both its browser (Internet Explorer) and its operating systems (such as Windows 2000). Although Judge Thomas Penfield Jackson's findings against Microsoft have not survived on appeal, perhaps the most interesting thing Judge Jackson got wrong was that he completely missed the most significant development in the software business since the personal computer—the rise of open-source software.

Open-source software is software that is made freely available, including its source code (the programming instructions), to anyone who wants it, subject only to the requirement that the user make any enhancements he adds equally freely available. The open-source movement grew out of the work of Richard Stallings and his Free Software Foundation, and Linus Torvalds and the operating system he created, Linux.

GNU and Linux are the results of individual efforts, but both are also the product of an amazing spontaneous order. In these and other cases an initial piece of code was created by one person. That code was then made available to others, with the promise that updates would also be freely available. Thousands of programmers from all around the world became involved in solving problems and extending the programs. The originators then incorporated the suggestions into the programs and reissued new versions. Stallings, a brilliant programmer, created GNU, a freely available set of software for Unix systems. Even more important, Stallings created the GNU "copyleft" license that ensures that any software created using GNU would itself be freely available.

Open-source software has evolved into a potent threat to closed-source software, like Microsoft's. As the book documents, companies—including Sun, Netscape, and IBM—have embraced the open-source model for a variety of programs. Strikingly, for example, Torvalds built a barely functional Unix-like operating system from scratch as a hobby project. Through releasing the code, he evolved it into a major operating system in use around the world today—and one that remains freely available to all. Other companies have built businesses out of providing support for open-source programs—most notably Red Hat Software, one of the major suppliers of Linux.

In *Rebel Code*, Glyn Moody (a contributor to *Wired* and similar publications) has written a compelling account of the rise of the open software movement. Moody interviewed many of the most important participants, including Torvalds, Stallings, and Eric Raymond. (Raymond's essay, "The Cathedral and the Bazaar," available in book form or on numerous websites, is the best introduction to open-source ideas.) Moody explains the technical stuff clearly and frequently enough for a nonhacker to follow. Although at times he drifts into excessive detail on participants' personal lives and uncritical appraisal of individuals, he successfully presents all sides of the major disputes within the open-source movement.

This is an important book for libertarians to read for three reasons. First, intellectual property (IP) presents tough issues for libertarians. Some libertarians support treating IP like other forms of property; others do not. The success of open-source programs poses an important question for those who attempt to justify IP on utilitarian and economic grounds. If GNU/Linux can succeed, then the "we must protect IP or no one will produce it" argument is significantly weakened.

Second, the programmers involved in open-source projects are a group to which we need to present our ideas. Many of the



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ideas behind the open-source movement are similar to ideas critical to libertarian thought—spontaneous order and freedom. As the open-source movement grows, persuading its adherents like Eric Raymond to pay attention to the works of F.A. Hayek, Ludwig von Mises, and others may bring us important allies.

Finally, there is a struggle over the future of the Internet happening now. The open-source movement is a powerful force for liberty on the Internet—Eric Raymond's website has a link to decryption code that the motion picture industry is attempting to stifle through lawsuits. Open-source programmers occupy positions of authority at many corporations and institutions and are in a position to resist attempts by governments to seize control of the basic functions of the Internet to allow censorship and worse. We need to understand this movement so that we can call for help when we perceive a threat to liberty.

This book (together with Raymond's essay and Neal Stephenson's fine novel *Snow Crash*) provides an excellent vehicle for us to educate ourselves. □

*Contributing editor Andrew Morriss is Galen J. Roush Professor of Business Law and Regulation at Case Western Reserve University, Cleveland, Ohio, and a senior associate at PERC—the Center for Free Market Environmentalism.*

## Money & Power: The History of Business

by Howard Means

John Wiley & Sons, Inc. • 2001 • 274 pages • $27.95

*Reviewed by John Hood*

Television can be not only entertaining but educational, as long as you are not seeking great depth or elaborate argumentation. That means that it's possible to adapt excellent writing for television but not the reverse. In *Money & Power: The History of Business*, author Howard Means has adapted a CNBC documentary into a book that provides little of value to one seeking a serious treatment of business history. The breezily written book manages to be insubstantial and infuriating at the same time.

Means attempts to tell the history of business through a series of essays on famous individuals or episodes. The choice of subjects is predictable; the Medicis, the tulip bubble, J.P. Morgan, John D. Rockefeller, and so on. Unfortunately, so is the sorry economic analysis. Means indulges in the usual demonization of entrepreneurial effort, characterizing innovation as "cutthroat competition" and employing loaded terms like "robber baron" with little regard for fine distinctions or economic rationality. It's the kind of book that has been misleading Americans about the role and nature of business for generations.

The essay on Rockefeller is particularly galling. Means indulges in various tirades about Rockefeller's "ruthlessness and unsentimentality" (meaning his relentless efforts to reduce the price of oil, that scalawag!) and his corrupt "buying" of the politicians of the day. These were the same politicians who had erected the trade restrictions that Rockefeller's trusts and other innovations were meant to evade. Paying intrusive or tyrannical politicians to leave him alone probably seemed to Rockefeller to be a perfectly reasonable expenditure of his and his shareholders' money. Means can only see corruption, missing entirely the fact that the evasion of anticompetitive regulations was economically beneficial.

If Means had really wanted to tell the story of the history of business, he might have explained Rockefeller's dilemma in greater detail. Before inventing the modern trust, he had already amassed a considerable fortune by refining and marketing oil more efficiently than anyone else. One secret to his success was a waste-not strategy that sought to use every by-product of the refining process. His chemists came up with 300 different uses for a barrel of oil. Rockefeller also pioneered vertical integration. His partnership with Henry Flagler and Samuel Andrews not only refined oil but also harvested and dried timber, transported it to



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factories, and then produced the barrels necessary to haul the oil.

Five years after the founding of their refining plant in 1865, the price of kerosene had dropped by 50 percent. Rockefeller's ceaseless pursuit of lower prices drove other refiners out of business, many of which he then acquired. By 1880, his company controlled 80 percent of the kerosene business. Contrary to the predictions of those with a simplistic view of markets, such as Means, Rockefeller could not then rest on his laurels and run a high-priced monopoly. Kerosene itself had competitors, including whale oil and electricity. Furthermore, there was always the possibility of new entrants to the kerosene market. So Rockefeller pushed on. By the time the company reached 90 percent of market share five years later, it had driven prices down another 69 percent, to 8 cents a gallon.

Although hardly helpful to Rockefeller's competitors, his business acumen was immensely beneficial to industry as a whole and to the American (and world) consumer. But does Means undermine his attack by mentioning the fact that Standard Oil made life much better for the consumer? Of course not.

On the other hand, Means seems to vindicate him only by reporting what, to Means at least, was a puzzling contradiction: Rockefeller's philanthropy. The implicit message is that making lots of money is bad, but at least it can then be given away.

Means does the same for Henry Ford, whom he badly maligns, by explaining that the Ford Foundation's "general support for a variety of liberal and social-welfare programs (causes Ford himself might well have loathed) would help buff the image of the automaker."

Are we to understand that an entrepreneur who created his great fortune by serving humanity well, through innovation and hard work, needed his image improved by having his fortune squandered by others, against his expressed wishes, on left-wing projects of dubious merit?

Anyone who would suggest such a thing lacks the insight necessary to explain the history of business. Others have performed the task far better, including Gerald Gunderson's excellent *The Wealth Creators* and Larry Schweikart's *The Entrepreneurial Adventure: A History of Business in the United States.*

Read those books and skip the disinformative *Wealth and Power.* □

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*John Hood is president of the John Locke Foundation, a public-policy think tank in North Carolina. His books include* The Heroic Enterprise: Business and the Common Good *(The Free Press, 1996) and* Investor Politics *(Templeton Foundation Press, 2001).*

## Absolute Power: The Legacy of Corruption in the Clinton-Reno Justice Department

by David Limbaugh

Regnery Publishing • 2001 • 385 pages • $27.95

*Reviewed by Arch T. Allen*

"Power tends to corrupt, and absolute power corrupts absolutely." Lord Acton's famous admonition underlies both the title and subtitle of this account of how President Clinton's promised "most ethical administration" in American history came to include a politicized and corrupt Justice Department. Critical of Clinton and Janet Reno, his appointed attorney general to head the Justice Department, author and attorney David Limbaugh describes and documents their politicized corruption of the administration of justice.

The U.S. Constitution vests federal executive power in the president, who is under oath to execute the office faithfully and to preserve, protect, and defend the Constitution. Among the president's constitutional duties, he shall take care that the laws be faithfully executed. Underlying those constitutional provisions is the political philosophy of protecting liberty through the rule of law. As Limbaugh notes, the rule of law is the core maxim "that we are a government of laws, not men." Accordingly, no man is above the law, and the law restrains the government itself. Nevertheless, what James



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Madison called "the great difficulty" remains: "You must first enable the government to control the governed; and in the next place oblige it to control itself."

Limbaugh "bookends" his case against Clinton-Reno abuse of the governed with accounts of the Waco disaster and the Elián González abduction. At Waco, agents of the Clinton-Reno Justice Department executed a military-style seizure of a sect's compound under the pretense of serving search and arrest warrants, resulting in the deaths of scores of American citizens including children. In Elián's case, other Clinton-Reno agents executed a pre-dawn commando-style raid of an American home under the pretense of a search warrant to abduct a legal-alien child at gunpoint, resulting in his return to communist Cuba. In both cases, Clinton and Reno piously proclaimed the primacy of the rule of law, but, as Limbaugh demonstrates, the law required neither the Waco seizure nor the Elián abduction; they were Clinton-Reno decisions.

Between those bookends, Limbaugh chronicles the Clinton-Reno failure to apply the rule of law to themselves and their government. He shows how political expediency led Reno to abandon an earlier legal position and undertake unprecedented litigation against an American business, how opportunism and cronyism led to a conspiracy against innocent government employees, how the politics of personal destruction led to the release of an employee's personnel records in violation of privacy protections, how far-fetched privilege claims were asserted to delay investigations, how administration lawyers ignored or avoided some Supreme Court interpretations of the Constitution, and how Clinton granted clemency to terrorists in an obvious effort to bolster his wife's senate campaign.

In Limbaugh's most devastating accounts, he explains the Clinton administration's compromise of American security in soliciting Chinese political contributions to his re-election campaign and how Clinton and Vice President Al Gore illegally raised political contributions. And he shows how Reno enabled them to avoid enforcement of the laws against them by preventing career Justice Department personnel from pursuing the matter under the pretense that it might become subject to an independent counsel—and then refusing to appoint an independent counsel. Limbaugh leaves no room to doubt that politics was often the deciding factor in Justice Department action or inaction.

The author exposes the Clinton-Reno "rule of law" as a pious pretense masking political opportunism and depending, to borrow Clinton's infamous phrase, "on what the meaning of is is." Americans who cherish their liberty under the rule of law should lament that more of us are not as concerned as David Limbaugh about the Clinton-Reno abuses. The politicization of the Justice Department is something much to be regretted, as it removes one of the obstacles to wrongdoing by the president and his administration. With the Justice Department in the hands of dutiful party men (or women), the executive branch is not "obliged to control itself." Alas, Bill Clinton has now set a precedent in that regard.

*Absolute Power* is a polemic, however, and as the brother of Rush Limbaugh, the author is subject to familiar dismissal as just another "a Clinton hater." That evasive tactic, however, should not dissuade people from reading this serious and well-researched book. □

*Arch Allen is a lawyer in Raleigh, North Carolina.*

## The Cash Nexus: Money and Power in the Modern World, 1700–2000

by Niall Ferguson

Basic Books • 2001 • 425 pages • $30.00

*Reviewed by Martin Morse Wooster*

Niall Ferguson, an Oxford University historian, is best known for *The Pity of War*, a book arguing that it was a mistake for Britain to enter World War I. But he is also a financial historian, whose most lengthy book is a two-volume history of the Rothschild banking dynasty. In his latest



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book, Ferguson engagingly examines three centuries of European and American financial history in search of economic trends. Although some of his conclusions are debatable, Ferguson is a lively and intelligent writer whose research once again confirms that, left unchecked, government will grow endlessly.

In many ways, *The Cash Nexus* is a conservative response to *The Rise and Fall of the Great Powers*, a 1988 work by historian Paul Kennedy that contended that the United States, by spending too much money on the military, was suffering from "imperial overstretch" and would lose the economic war with Germany and Japan. Ferguson argues that, after the Cold War, the reverse is true—that an American elite afraid of causalities in foreign wars is abandoning its role as the world's policeman. "The leaders of the one state with the economic resources to make the world a better place lack the guts to do it," he writes.

Readers who wonder why the United States should in any way interfere in the domestic politics of Yugoslavia, Somalia, or Haiti should, however, realize that Ferguson's saber-rattling accounts for only two chapters of this lengthy work. The rest of the book, which describes the role that economics plays in politics, is one that market-oriented types should find quite congenial.

*The Cash Nexus* explores many economic topics. Among them are whether or not rising incomes advance democracy; the role economics plays in elections; the origins of national debt and the influence of the bond market in politics; the connections between inflation and political instability; and the relationship between the business cycle and politics. The result is a book that more closely resembles a public-policy book with historical examples than a more conventional history.

In less skillful hands, *The Cash Nexus* could have been dull. But Ferguson is an excellent writer who is good at unearthing illuminating anecdotes. He also has a gift for comedy. For example, when discussing gold, Ferguson begins by summarizing the section of Ian Fleming's *Goldfinger* in which James Bond, "whose ignorance of monetary matters outside the casino is more or less complete," is lectured by a representative of the Bank of England on the importance of gold to the British economy.

Perhaps Ferguson's most interesting research is on the origin of democracy. Many of us were taught that democracy arose because the people were disgusted by the tyrannies of unaccountable monarchs and demanded a say in how they were governed. But Ferguson shows the state's hunger for taxes played a more crucial role.

In the Middle Ages, taxation tended to be the royal prerogative, thanks to "the royal domain," a system of state-owned monopolies. But monarchs needed to raise revenue for war, so they ended up selling most of these monopolies to pay the troops. For example, when Henry VIII closed and seized Britain's monasteries in the 1530s and 1540s, he wasn't just stressing the independence of the Church of England; he also wanted the revenue from the Catholic Church's properties. But by the time Henry's son, Edward VI, became king in 1547, nearly seven-eighths of this land had been sold to pay for military campaigns.

Ferguson shows that new forms of taxation (such as income tax) were controlled by parliaments, which tended to gain power as their control of taxation increased. He also notes a strong correlation between easing the requirements to vote (such as allowing people to vote who weren't property owners) and the rise of the state. Many of the newer voters had incomes so low that they didn't have to pay income taxes, so they constantly agitated for taxes to be raised on richer Britons in order that they would get more government subsidies. By 1913 Sir Bernard Mallett would argue that in democratic Britain, public policy was determined by "an electorate consisting mainly of the poorer classes, while revenue is obtained mainly from a minority of wealthier persons." The tendency of government to tax the rich to reward the indolent, argues Ferguson, has only increased with the rise of the welfare state.

There is much more intelligent analysis in



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*The Cash Nexus*, from how increased taxation caused the creation of government bureaucracy to the ways the international bond market redistributes wealth from poor taxpayers to wealthier bondholders. Ferguson is an independent voice, generally skeptical of the excuses politicians make for raising taxes or bloating government. The lasting lesson his pioneering work provides is that raising taxes is, for most politicians, an action as natural as breathing or eating. □

*Martin Morse Wooster is an associate editor of* The American Enterprise.

## The Virtue of Prosperity

by Dinesh D'Souza

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• $26.00 paperback

*Reviewed by George C. Leef*

The Harvard economist Joseph Schumpeter famously predicted that capitalism, in so greatly magnifying man's productive capability, would sow the seeds of its own downfall by creating an idle class of malcontents who would undermine the philosophical foundations of the economic order built on individual rights. The first part of his argument has certainly come true. Thanks to capitalism, more people now live comfortably than ever before, and by a wide margin. Schumpeter was also right in predicting the rise of grumblers who would incessantly find fault with the material progress of capitalism. We don't yet know whether they will in fact bring about the downfall of the free-market system, but they're working at it.

Dinesh D'Souza's book *The Virtue of Prosperity* examines the arguments made by both the socialist critics of capitalism who can't abide inequality and the cultural conservative critics who don't like the effects of capitalism on the values they hold dear. D'Souza has a knack for grabbing hold of hot issues and saying sensible things about them—his earlier books *Illiberal Education* and *The End of Racism* being cases in point. He has done so again here, subjecting the rhetoric of leftist and rightist critics to penetrating scrutiny.

The author sees the conflict as dividing along these lines: There are those who are pleased with the fabulous prosperity and progress brought about by the workings of capitalism, want more of it, and harbor neither resentment that others have gotten richer than they have nor worry that prosperity is somehow undermining "deeper" values. D'Souza calls them The Party of Yeah. On the opposite side are those who are upset about the success of capitalism. D'Souza calls them The Party of Nah. The Party of Nah then divides into leftist and rightist branches as noted above. The book is an attempt to find out just what the various factions are saying, and whether we should take to heart any of the Party of Nah attacks. (The answer D'Souza gives is no, but with some equivocation.)

George Gilder is a good example of a Party of Yeah member. D'Souza writes, "In Gilder's view there is virtually no downside to the proliferation of technological capitalism." Its prospects for improving the human condition are breathtaking. In Gilder's own words, "The new age of intelligent machines will enhance and empower humanity, making possible new ventures and new insights. It will relieve man of much of his most onerous and unsatisfying work. It will enlarge his freedom. It will diminish despots and exploiters." To those who scoff at such claims, D'Souza replies that capitalism and its technology have a mighty impressive performance record. Look back over the last century and you will see accomplishments that were laughed at as impossible by most people. All are attributable to Party of Yeah endeavors.

Sneering in derision, however, are the likes of Studs Terkel, an old leftist grumbler who can only see that some people are getting exceedingly wealthy. "But what pisses me off is what happens to the people at the other end of the line," he says. "People are struggling to make ends meet in this country. Out there in the world millions are scrounging for something to eat. Is it right that so



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many people are starving while these guys have more money than God?" Lines like that still get you invited to give talks on college campuses, but should sensible people worry about the allegedly expanding wealth gap? D'Souza thinks not, pointing out that capitalism has single-handedly made it possible for millions of poor people around the globe to lead longer, healthier lives. In his estimation, it's silly to complain about relative wealth as long as absolute wealth is rising for nearly everyone.

The anti-capitalist sentiment from the conservatives isn't based on inequality, but rather on the supposedly harmful impact capitalism has on social morality. D'Souza quotes Gertrude Himmelfarb: "Economically, our society is better off. But in many ways we are a much poorer society than we used to be. There are other forms of poverty than economic poverty, you know." He doesn't have much sympathy for this line of attack either, which he finds rooted in the philosophy of antiquity that the principal task of the state was the promotion of virtue. Critics like Himmelfarb, William Bennett, and Robert Bork complain that capitalism, while providing a high standard of living, also provides bad things and subverts morality. D'Souza doesn't see that there is anything the state can do about that without unleashing worse problems. Besides, he observes, techno-capitalism is making it possible for parents to spend more time with their children, allowing them to promote the values they think important.

The one issue where the author expresses some Nah-ism is in his discussion of the possibility of bioengineering human beings. He wants to ban it, writing, "when we start remaking human beings, then I think we have crossed a new and perilous frontier." D'Souza's thoughts here strike me as far from convincing, but they should not deter one from taking up this sprightly book on one of the key intellectual battlegrounds of the 21st century. □

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*George Leef is book review editor of* Ideas on Liberty.



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# Government-Sector Unionism

In my February column I gave two examples of the decline of unionism in the private sector and pointed out that the picture is very different in the government sector. Whereas the unions' private-sector market share in 2001 was 9 percent, in the government sector it was 37.4 percent (down slightly from 37.5 percent in 2000). What accounts for the relative success of unionism in the government sector, and what unique constitutional issues emerge therein?

First, unions are organizations that try to quash competition among workers in the job market. In short they are, or try to become, labor monopolies. A monopolist in the production and sale of a product tries to restrict its supply and increase its price above competitive levels. A union tries to restrict the supply of labor and increase its wage above competitive levels.

Private-sector employers usually try to avoid paying supra-competitive wages because they cannot easily pass the resulting cost increases on to their customers. Their customers typically have many alternative vendors with which to do business. Government-sector employers, on the other hand, are often monopoly providers of their (alleged) goods and services. Their "customers" (taxpayers) do not have alternative vendors to which to turn. Moreover, their customers cannot refuse to pay the prices (taxes) the government agencies charge them. Thus government-sector employers can, much more easily than private-sector employers, pass forward any cost increases that result from paying supra-competitive wages, and therefore they do not resist union demands at the collective bargaining table as much as private-sector employers do.

Second, government-sector workers realize that the determination of taxes and spending is a political process, and they know that organized interests are more successful in the political marketplace than unorganized individuals. Claims by government employee unions (GEUs) to be able to improve terms and conditions of employment for their members have more credibility than similar claims in the private sector, so government-sector workers are more receptive to union organizing than private-sector workers.

Finally, the two sides of government-sector collective bargaining have a common interest—to pick the taxpayers' pockets. Government agency heads are empire builders. They want more visibility, authority, and responsibility, and larger budgets than they have. They are perfectly happy to cooperate with GEUs in pursuing those ends. For example, administrators and faculty unions at government universities often join forces in lobbying legislatures for bigger university budgets. They may fight over their respective shares of those budgets, but they agree that bigger budgets are better than smaller budgets.

The state statutes that control unionism for state and local government employees

*Charles Baird (cbaird@bay.csuhayward.edu) is a professor of economics and the director of the Smith Center for Private Enterprise Studies at California State University at Hayward.*



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are all patterned after the National Labor Relations Act (NLRA), which controls all private-sector unionism. Three features of the NLRA are particularly odious when applied to government employment—exclusive representation, union security, and mandatory good-faith bargaining.

*Exclusive representation* means that a union selected by a majority of a company's employees in an election is the monopoly representative of all who were eligible to vote. Individuals are even forbidden to represent themselves on issues of wages and other terms and conditions of employment. I have often argued that even in the private sector exclusive representation violates individual workers' freedom of association. The Supreme Court disagreed by saying that the government is not a party in private-sector collective bargaining so the Bill of Rights, which limits government encroachments on individual freedoms, does not apply. I think the Court is wrong because Congress created the NLRA and is therefore a party to all of its processes. Be that as it may, with government-sector collective bargaining, governments are indisputable parties. Therefore, granting exclusive representation to GEUs is unconstitutional on its face because governments discriminate against workers on the basis of association (or lack thereof).

## Preventing Free Riding

*Union security* means that all workers represented by a certified union must pay fees for the "service." Unions say they need union security to prevent individuals from free riding. Whether in the private or government sector, the unions' free-rider problem is an artifact of the law. Without exclusive representation there could be no free riders. However, in the government sector, governments are parties to the collective-bargaining agreements that include union-security clauses. A government that imposes union security thereby threatens to fire employees who do not pay a tax to the GEU. This, too, is clearly government discrimination against workers on the basis of their association (or lack thereof) with a private group. It is also a grant of taxing power to private groups. It cannot withstand objective constitutional scrutiny. The Court has recognized this problem with GEUs, but has said the denial of freedom of association must be balanced against the government's interest in maintaining labor peace. The Court ignores the fact that the granting of monopoly privileges almost always results in less labor peace. Politics dictates that GEUs must have union-security privileges, and the Court simply fabricated a particularly silly argument to excuse it.

*Mandatory bargaining* requires that if either the employer or a certified union wants to bargain about some labor-related issue, the other side must agree to bargain about it. Moreover, the bargaining must be in good faith, which in practice means each side must make concessions to the other. The only sure defense against an accusation of failure to bargain in good faith is a record of compromise.

In the government sector, wages and other employment conditions are matters of public policy. Mandatory good-faith bargaining with GEUs means that governments share the making of public policy with private groups. This, in effect, creates a fourth branch of government contrary to the Constitution. Of course, all sorts of private groups attempt to influence public policy by lobbying and making campaign contributions, but GEUs are special: it is illegal for politicians and agency heads who are in collective bargaining with GEUs to ignore them. Thus GEUs have the legal power to veto government policy. This is the clearest case of the unconstitutional delegation of government authority to private groups I can imagine. Yet, here again, the Court has been willing to permit violation of the Constitution in the name of political expediency.

Government-sector unionism is the only hope that union sympathizers have that unions will not eventually become irrelevant. It is also the form of unionism that is most clearly unconstitutional. If the Supreme Court ever summons the courage to once again defend the Constitution, unionism will become a curious historical relic. □



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*"Why, when I think of those multitudes of clerks and congressmen—whole families of them—down there slaving away and keeping the country together, why then I know in my heart there is something so good and motherly about Washington, that grand old benevolent National Asylum for the Helpless."*

—MARK TWAIN (1835-1910), *The Gilded Age* (1873)

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